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SUBCOMMITTEE ON
COAST GUARD AND NAVIGATION

OF THE

COMMITTEE ON
MERCHANT MARINE AND FISHERIES
HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRD CONGRESS

SECOND SESSION

ON

THE COAST GUARD'S INTERIM FINAL RULE ON REQUIREMENTS FOR EVIDENCE OF FINANCIAL RESPONSIBILITY UNDER THE OIL POLLUTION ACT OF 1990

JULY 21, 1994

Serial No. 103–123

Printed for the use of the Committee on Merchant Marine and Fisheries

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VESSEL CERTIFICATES OF FINANCIAL RESPONSIBILITY

THURSDAY, JULY 21, 1994

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COAST GUARD AND NAVIGATION,
COMMITTEE ON MERCHANT MARINE AND FISHERIES,
Washington, DC.

The Subcommittee met, pursuant to call, at 10:00 a.m., in room 1334, Longworth House Office Building, Hon. W. J. (Billy) Tauzin (Chairman of the Subcommittee) presiding.

Present: Representatives Tauzin, Lancaster, Barlow, Pickett, Laughlin, Taylor, Coble, Bateman, and Gilchrest.

Staff Present: Subcommittee—Elizabeth Megginson, Catherine Tucker, Bill Wright, Jim Adams, Douglas Cheramie, Sharon Donald; Full Committee—Tom Kitsos, Sue Waldron, Joan Bondareff, Lee Crockett; Minority—Harry Burroughs, Cyndi Wilkinson, Ed Lee, Rebecca Dye, and Margherita Woods.

STATEMENT OF HON. W.J. TAUZIN, A U.S. REPRESENTATIVE FROM LOUISIANA, AND CHAIRMAN, SUBCOMMITTEE ON COAST GUARD AND NAVIGATION

Mr. TAUZIN. The hearing will please come to order.

We may have a journal vote this morning. I think that is why Members are holding back. Mr. Coble and I will get our statements in and hopefully we will not have to interrupt the hearing in that regard.

We welcome you to this hearing of the Coast Guard and Navigation Subcommittee. The subject of this hearing is the Coast Guard's interim final rule on the requirements for evidence of financial responsibility under the Oil Pollution Act of 1990. We will focus on this rule, its impact, and the implementation of the regulation.

As I have stated before, I think it is important for this subcommittee not only to pass legislation, but also to oversee the implementation of the law through the regulatory process. When the Oil Pollution Act of 1990 was signed into law, we in Congress all shared the same goal of ensuring that oil spills are prevented. However, recognizing the inevitability of error in the event of an oil spill, we wanted to ensure that sufficient resources are available to promptly and fully respond.

As you may recall, this subcommittee held hearings on the proposed rule in November of 1991. It almost seems like ages ago. It seems like we were on the moon more recently than our last hearing.

At that hearing, we heard concerns about whether there would be insurance available to cover the risks of an oil spill. During that hearing, I asked the Coast Guard to work with the parties involved to arrive at a mutually acceptable set of solutions with an interim final rule published. It is now time again for this subcommittee to review the rule and hear from the involved parties as to how it will affect them, and more importantly, how it will affect this country and the consumers of energy dependent upon the system of transport.

It is important that we learn today what this will cost the Coast Guard, the industry, and the consuming public. Is it a reasonable set of rules? Will there be adequate time to allow new guarantor entities to develop and to provide the evidence of insurance coverage for vessels entering U.S. waters by December 28, 1994? Concerns have been expressed that the Coast Guard is depending on the development of new guarantor entities to provide the evidence of financial responsibility.

We don't know at this time whether or not or to what degree these entities will be able to provide these guarantees and, indeed, service the entire market. The Coast Guard needs to proceed, as we have said before, cautiously to ensure adequate coverage and the full ability to provide a response to a spill at reasonable cost to all parties.

The very last thing our country needs is the possibility of a disruption in supplies of the extremely important various products coming to the United States covered by the OPA 90 law and regulations.

I am pleased now to recognize the Ranking Minority Member, my good friend with whom I share responsibility for this Subcommittee and for whom I thank again for his extraordinary bipartisan cooperation with the chair and with the full committee in his work, Mr. Howard Coble.

STATEMENT OF HON. HOWARD COBLE, A U.S. REPRESENTATIVE FROM NORTH CAROLINA, AND RANKING MINORITY MEMBER, SUBCOMMITTEE ON COAST GUARD AND NAVIGATION

Mr. COBLE. I thank you, Mr. Chairman.

I appreciate your calling this hearing regarding the recently released Coast Guard interim final rule, which will implement the financial responsibility provisions for vessels under the Oil Pollution Act of 1990. I realize that the Coast Guard has spent several years attempting to develop a plan which provides a way to guarantee that vessel owners and operators pay for future oil spills, popularly known as "polluter pays". I certainly support the goal of having the polluter pay for his own pollution.

However, the Congress cannot allow a situation to develop, in my opinion, where the lack of availability and/or excessively high cost of oil vessel liability insurance stops the flow of oil into our country. Such a scenario would quickly devastate our economy.

The Coast Guard's detailed Regulatory Impact Analysis concludes that the rule will not cause severe economic disruption, since the two commercial enterprises have indicated that they can provide the necessary guarantees to ship owners and operators. I

am advised that a representative from one of these new ventures, Shoreline Mutual Management, will testify today. I will be particularly interested to hear about Shoreline's efforts to raise the necessary capital to operate, as well as the estimated cost of this future financial guarantee.

I also look forward to hearing, Mr. Chairman, whether the other witnesses who represent the world's oil, insurance, and oil transport industries, think they will be able to operate under this new rule.

I thank the Chairman.

Mr. TAUZIN. I thank you, Mr. Coble.

Mr. Fields has a statement he would like to submit, so without objection, it will appear in the record.

[The statement of Mr. Fields follows:]

STATEMENT OF HON. JACK FIELDS, A U.S. REPRESENTATIVE FROM TEXAS, AND RANKING MINORITY MEMBER, COMMITTEE ON MERCHANT MARINE AND FISHERIES

Mr. Chairman, nearly four years ago I was a member of the Conference Committee that developed the Oil Pollution Act of 1990 (OPA '90). At that time, I strongly supported implementation and ratification of the 1984 International Oil Spill Protocols to provide a reasonable, predictable limit of liability to vessel owners for oil pollution damages.

The International Protection and Indemnity Clubs also strongly advocated adoption of the International Protocols. They informed the OPA '90 Conference Committee members that they would not act as guarantors under OPA '90 if the U.S. did not ratify the Protocols. Unfortunately, the Senate blocked ratification of the Protocols, because they objected to a national limit of liability. Chairman Studds proposed compromise legislative language to implement the Protocols that solved 99 percent of the concerns of the opponents. Regrettably, that proposal was not seriously considered by the Senate conferees, and vessel owners and the Coast Guard were left with no place to turn for coverage for oil pollution damage.

I am terribly concerned that the Coast Guard has chosen to implement the interim final rule for certificates of financial responsibility in such a short time frame. It took the Coast Guard four years to develop this rulemaking, and there is no reason now to rush implementation. Although Shoreline Mutual is attempting to raise the necessary capital investment to issue certificates of financial responsibility under OPA '90, they are still not ready to issue those certificates. This has put oil transporters in a terrible position: in six months, they must find oil spill coverage, or be out of business.

Another concern of mine is the cost of oil spill coverage under OPA '90. I have heard that the cost of coverage under the Coast Guard's interim final rule will be 7 to 9 times more than existing rates. A constituent of mine told me that his coverage under the Coast Guard final rule would cost $1 million per voyage!

Mr. Chairman, clearly, we made a mistake in 1990 by refusing to deal squarely with this issue. I hope the Senate understands the seriousness of this problem, because any disruption of oil transportation this winter could have widespread ramifications. We still have a chance to correct this problem and deal with reality by ratifying the 1992 Oil Spill Protocols which would ensure the continuation of safe, efficient transportation of oil in this country.

I look forward to hearing from today's distinguished witnesses and I will continue to vigorously support efforts to solve this serious problem. I remain convinced that we can protect our fragile coastal investment without displacing dozens of oil transporters.

Thank you, Mr. Chairman.

Mr. TAUZIN. The committee will hear three panels of witnesses and the first witness will be Admiral Robert Kramek of the United States Coast Guard, Commandant of the Coast Guard, accompanied by Mr. Daniel Sheehan and Mr. Robert Horowitz.

It is my understanding we do have a roll call vote that has been called on the journal. It had been my hope that we might have someone here who might continue the proceedings. Since they are

not here, it will be necessary that Mr. Coble and I recess the hearing for this vote. We will be back in approximately ten minutes.

The committee stands recessed for about 10 minutes.

[Recess.]

Mr. TAUZIN. The committee will please come back to order.

Like that story in the Bible when you invited folks to show up and nobody came, and so you went and got more. We should have a few Members joining us after this roll call is finished, but we want to proceed so that we can expeditiously hear from the many folks who have traveled a long distance to share their thoughts on the record today.

We welcome Admiral Robert Kramek who is accompanied by Mr. Daniel Sheehan, Director of the National Pollution Funds Center and Mr. Robert Horowitz, Chief of the Regulation and Legislation Branch of the National Pollution Funds Center.

Admiral, I understand that you have to leave after your testimony, so I wanted to accommodate you as best we could. We welcome you to the Subcommittee and expect that we are going to have many times together. We hope this one is an enjoyable occasion for you. The Commandant of the United States Coast Guard, Admiral Kramek.

STATEMENT OF ADMIRAL ROBERT KRAMEK, COMMANDANT, UNITED STATES COAST GUARD, ACCOMPANIED BY DANIEL SHEEHAN, DIRECTOR, NATIONAL POLLUTION FUNDS CENTER, AND ROBERT HOROWITZ, CHIEF, REGULATION AND LEGISLATION BRANCH, NATIONAL POLLUTION FUNDS CENTER

Admiral KRAMEK. Good morning Mr. Chairman. It is a pleasure to be here this morning to testify before you and address the interim rule for certificates of financial responsibility. On my right is Dan Sheehan and on my left is Robert Horowitz, experts who have spent the last three years developing every aspect of this rule.

Dan is the Director of the National Pollution Funds Center and does more than just work on the COFR issue. The newspapers refer to him as the billion dollar man because he is the guardian of the Pollution Fund. The Coast Guard, as you know, has published an interim rule to implement the financial responsibility provision of the Oil Pollution Act of 1990, and CERCLA. I believe the rule implements the law as intended by Congress and balances the interests of the United States citizens and the maritime industry.

After the Exxon Valdez tragedy in 1989, OPA 90 was enacted by Congress and signed into law. The liability and compensation provisions of OPA 90, however, had been under development for many years prior to that, as you know.

There were many objections to adoption of that law and the proposed law's liability and compensation provisions, so Congress unanimously adopted a liability and compensation regime based on the fundamental concept that the polluter pays for removal costs and damages. In September 1991, the Coast Guard proposed a rule to implement OPA 90 and CERCLA's financial responsibility mandates, but was immediately challenged by the international ship-

ping industry for failing to use the rule to insulate that industry from the potential for unlimited liability.

As you mentioned, you held a hearing at that time which thoroughly reviewed the issues and concerns. The industry debate and administration debate has continued for almost three more years. But during that time, OPA 90 was not altered to authorize the Coast Guard to insulate the shipping industry from the possibility of unlimited liability. Accordingly, on 1 July, I signed the interim final rule.

This rule implements OPA 90's and CERCLA's mandate to protect U.S. taxpayers. It does this by enhancing the ability of a claimant to obtain compensation for removal costs and damages, suffered as a result of an oil spill or hazardous substance release, from the polluter or the polluter's guarantor. The rule adopts the themes of the notice of proposed rulemaking, but makes a number of technical improvements in response to comments.

And, Mr. Chairman, we have heeded your charge in 1991 to try to be as flexible as possible, to work together as best we can to get a mutually acceptable rule to all parties. I believe we have done this. That is why it has taken so long.

We have been as flexible as the law allows, in my opinion. But I know everybody is not happy.

I want to congratulate you on holding this hearing. I think it is very, very important to hear from all sides, to see exactly where we are, to measure the progress that we have made in coming up with a rule that we feel is as flexible as the law allows at this time.

The changes we have made since 1991, while technical, also enhance the statutory protections afforded guarantors. It phases in compliance, it permits financial responsibility to be demonstrated through time-tested methods of self-insurance, guarantees of insurance, surety bonds or financial guarantees. It also permits a catch-all, other evidence guaranty.

To remain as flexible and responsible as possible, we have adopted an interim rule with a request for comments. This 90-day comment period closes on September 29th. Nevertheless, an interim rule is still a rule.

We solicited further comments because fine-tuning of the technical adjustments, if necessary, is more easily accomplished in an interim rule rather than a final rule, and I would hope it would be seen as a measure of our flexibility. We want to be as flexible as possible to make any changes that need to be made at the last minute.

An issue often raised, and perhaps the most contentious in the context of this rulemaking, was the assertion that guarantors are subject to unlimited liability and, therefore, could not underwrite this exposure.

I don't believe this is true. Congress explicitly limited a guarantor's liability to the amount of financial responsibility and no more. In the past 24 years in this country, we know of no instance in which the guarantor's limits have been breached. We believe amendments made to the guaranty forms will reinforce OPA 90's clear limitation on a guarantor's liability and increase the comfort zone for guarantors. We have also included specific defenses reinforcing OPA 90's protections for guarantors.

Mr. Chairman, the Administration has deliberated a long time because we wanted to be sure we were doing the right thing and not unreasonably prejudicing industry. We also wanted to assure ourselves that we did not stray from Congress' mandate in OPA 90.

As time has passed, we are more confident than before that we have made the right decisions. In the time since publication earlier this month, we have been encouraged by responses to our rule. We have talked to and briefed numerous individuals and groups, including the staffs of relevant congressional committees.

The Department of Transportation is committed to assuring the public understands this rule. This month the Secretary met with many of the same groups you have here today to ensure himself that the Coast Guard has taken into account all things that need to be considered and that the rule implements the law and intent of Congress.

The Coast Guard has worked hard as a broker to come up with this rule. If there was a way to find more flexibility for all concerned, the people at the table with me here this morning would have found it. They have dedicated their lives to this type of work.

Mr. Chairman, there are many issues to be discussed today. Again, I want to compliment you and the committee for continuing to assure that we have promulgated a rule that best serves our Nation. My experts and myself are ready to answer any questions you or the Members may have at this time.

[The statement of Admiral Kramek may be found at end of hearing.]

Mr. TAUZIN. Thank you, Admiral.

If we can get a layman's clear picture of where the rules now leave the situation, as compared to the initial hearing we had. As I understand it, you have, in this new rule, clearly defined the defenses that are not going to be waived, that are available to guarantors under the new set of regulations. Am I correct that any defense other than the ones listed are waived by virtue of these regulations?

Mr. SHEEHAN. Yes, sir, that is correct.

Mr. TAUZIN. Can you give us a quick list? What policy defenses are available to a guarantor under this rule that possibly was not under the old set of rules.

Mr. SHEEHAN. I would ask my project counsel to do that, since he drafted that particular provision. They are spelled out in the rulemaking. Mr. Horowitz.

Mr. HOROWITZ. The defenses that we have specifically listed included statutory defenses that are available. And we have tried to ensure that the defense that the guarantor's liability is limited to the amount of the guaranty is available in case a claim is made against the guarantor in excess of the amount of the guaranty.

Mr. TAUZIN. So that answers the question of unlimited liability, that the policy can in fact invoke the defense of limitation of coverage to the amount of the policy; correct?

Mr. HOROWITZ. That is right. The limitation is the amount of the guaranty; that is right.

We have also built in a defense with regard to a concern that guarantors might be subject to liability under State law, perhaps unlimited liability under State law as a result of executing the

OPA guaranty. We have built in a defense that says that the execution of the OPA guaranty is solely for OPA and CERCLA and shall not be used in a State court action. If a State court tries to assert jurisdiction over a guarantor on the basis of the execution of the Federal guaranty, the guaranty allows the guarantor to invoke that defense.

Mr. TAUZIN. I want to give you a specific example of how that might come into play. If a guarantor has not submitted to State jurisdiction, has not agreed to be a guarantor under State law and this rule now permits that policy defense to be asserted against the execution of a State law, what type of State law would not operate against that guarantor as a result of that defense?

Mr. HOROWITZ. My thought is that if a State enacts a law that says that a guarantor that provides an OPA guaranty automatically consents to jurisdiction of the State for a State law claim, that is the type of a situation where this defense could be invoked. That doesn't mean that a State, of course, having an independent basis for asserting jurisdiction over an insurer, can't do that because OPA does not preempt State law. That is a fundamental OPA precept, but we want to make it clear, that in executing the Federal guaranty, that alone does not act as a concession to State law jurisdiction.

Mr. TAUZIN. Specifically, if a guarantor wants to allege that the shipper has defrauded the guarantor in statements made with reference to the condition of the vessel or the operation of the vessel, is that a defense that is available to the guarantor?

Mr. HOROWITZ. Those would be in the range of the traditional policy defenses which would not be available.

Mr. TAUZIN. Which would not be available?

Mr. HOROWITZ. That is correct. The only defense in that situation would be the willful misconduct of the responsible party so if some misrepresentation rose to the level of willful misconduct, maybe that would be a defense. But traditional policy insurance defenses, would not be available.

Mr. TAUZIN. So if a guarantor became a guarantor under these rules and he did so under the belief that a vessel was constructed a certain way or operated in a certain way and that was erroneous, the guarantor would still be called to respond?

Mr. HOROWITZ. Yes.

Mr. TAUZIN. Would the normal policy defense of failure to pay a premium be listed as a defense assertable by a guarantor under this rule?

Mr. HOROWITZ. No, it would not be, though these are——

Mr. TAUZIN. So that in normal insurance practice, if I don't pay my insurance and never make my premium payment, as I have agreed to do, my insurance company would still cover me?

Mr. HOROWITZ. That is correct, for this guaranty.

Mr. TAUZIN. Can you explain to us why in your regulations you have chosen not to allow the guarantors these rather normal policy defenses?

Mr. HOROWITZ. Because the purpose of these regulations is to ensure that there are funds available in the event of an oil spill and those are the types of defenses which can be invoked to avoid that result. We felt that the purpose of ensuring that funds are avail-

able is not served by allowing those defenses. This is a guarantee, not an insurance policy, per se.

Mr. TAUZIN. Please explain the difference for us between what you consider a guaranty and an insurance policy.

Mr. HOROWITZ. Congress specifically in creating guarantor status for providers of financial responsibility was mindful of the fact that it wanted to ensure that funds would be available, and if the whole host of policy defenses could be invoked, that assurance would not be there and then U.S. taxpayers may be left paying the bill through the trust fund.

Mr. TAUZIN. You have obviously concluded that some policy defenses are OK and some are not.

Mr. HOROWITZ. That is correct.

Mr. TAUZIN. How did you decide that a policy defense that would not subject yourself to State jurisdiction was OK, and how that might not leave people uncovered. Yet at the same time, you do not allow a rather common policy defense—that the parties haven't paid the premium?

Mr. HOROWITZ. The policy defense for State law jurisdiction doesn't apply to OPA 90 and CERCLA, which are the measures that Congress has mandated here. We are not dealing with payments under State law. That is for States to deal with. We felt that it was very rational for us to insulate a guarantor in that case against the alleged potential for unlimited liability under State law. We are only looking for a Federal guaranty, not to ensure payments under State law.

Mr. TAUZIN. We have been told that there are some new lines of insurance. I understand that, according to the information that we received, these new lines of insurance have not in fact submitted a formal request to the Coast Guard to be found acceptable; is that correct?

Mr. HOROWITZ. That is correct.

Mr. TAUZIN. All we have is a possibility that they are going to be filing these requests and the possibility that they may be found acceptable?

Mr. HOROWITZ. That is correct.

Mr. TAUZIN. What we do know is that the current forms of coverage through P&I clubs, as you have indicated, can't or will not provide evidence of financial responsibility under these regulations. So, we are left with a situation where with the rules you have promulgated, the current customary form of coverage through P&I clubs may not be liable and likely not to be available. And the other new insurance forms have not yet filed with you, both you and I don't know whether they will, and whether you will accept them once they have filed. What have we wrought here?

Mr. SHEEHAN. Sir, I would like to respond to that. We went into this final—interim final rule looking at that possibility and certainly with the view that the P&I clubs would not change their stated positions they have put forward over the last three years and in response to the preliminary Regulatory Impact Analysis which we prepared in July and published. We received a wide range of comments because we looked at the economic impact of this particular rulemaking. And, we have on the docket two poten-

tial insurers who have indicated their willingness to step forward and come to the National Pollution Funds Center——

Mr. TAUZIN. Have they indicated what rates they are going to charge?

Mr. SHEEHAN. No.

Mr. TAUZIN. I am being told that it may be nine times what the shippers are paying now.

Mr. SHEEHAN. We have taken the conservative view of seven times.

Mr. TAUZIN. You have heard seven times.

Mr. SHEEHAN. That was a calculation that we did.

Mr. TAUZIN. Are you comfortable with placing the shipment of critical oil supplies for America in a situation where the current insurance forms may not be available and everybody may have to buy coverage at nine times—seven times current rates?

Mr. SHEEHAN. Mr. Chairman, as we indicated in the rulemaking, we do not believe that a train wreck is going to occur.

Mr. TAUZIN. I didn't ask you that. I said are you comfortable with the rules that currently seem to indicate that shippers are going to have to pay seven times as much for coverage as they formerly did.

Mr. SHEEHAN. Yes, sir, I am comfortable with the fact——

Mr. TAUZIN. Have you examined the economic impact on the consumers to America? What is that going to be, the total bill?

Mr. SHEEHAN. Our analysis indicated less that two-fifths of a cent at the pump.

Mr. TAUZIN. What is the total bill, Mr. Sheehan? Do you have it in dollars for us.

Mr. SHEEHAN. I do not have the total number.

Mr. TAUZIN. Has anybody done that in the Coast Guard?

Admiral KRAMEK. We have that and we request to provide that for the record.

[The information may be found at end of hearing.]

Mr. TAUZIN. I would suggest that we advertised this hearing for a long time. If the Coast Guard has done an economic analysis, it ought to be here today. Is anybody prepared to give us the number of the impact upon consumers in America of a seven-fold increase in the cost of coverage?

Mr. SHEEHAN. We did that in the final regulatory economic analysis. I don't have the number.

Mr. TAUZIN. Suppose somebody could get on the phone and get the number and give it to us today.

Mr. SHEEHAN. Yes.

Mr. TAUZIN. We will continue with other questions, but I would respectfully request——

Admiral KRAMEK. We boiled that down to the impact to the consumers of America to be two-fifths of one cent a gallon at the pump.

Mr. TAUZIN. I have heard that answer. My question was what is the total dollar impact as calculated in your economic analysis. You tell me that you have it but you cannot share it with us. When will you have it?

Mr. SHEEHAN. Before the hearing is over.

Mr. TAUZIN. When will the Coast Guard know whether these new forms of insurance will, in fact, be available to shippers?

Mr. SHEEHAN. The two entities at this point are putting together their plans. They have indicated that they are going to be coming into the Coast Guard for approval within the next two to three months. I have a meeting on Friday with the representatives of one of the organizations. We will put them through the standard review that we do with other insurers.

We also have the surety bond market which has come forward and said that they will provide surety bonds for the provision of certificates of financial responsibility. We have had a rather large increase in the number of inquiries about entities who would wish to self-insure.

Mr. TAUZIN. Well, if I am looking at a conservative timetable, you are telling me several more months before you know they are ready to submit. It is now approaching August. We have got a December timetable. I take it you cannot assure me that every shipper will be able to buy this insurance, even if they have to come up with seven-times current rates. How do we know that by December this thing will all be in place and working?

Mr. SHEEHAN. I think that we will have an indication in advance of the December 28th date.

Mr. TAUZIN. Like when? When will we be comfortable in knowing these new insurance forms that are going to replace the old insurance forms are, first, available to every shipper, second, acceptable by every shipper and, third, actually subscribed to by enough shippers to guarantee no interruption in supply.

Mr. SHEEHAN. I would indicate in the next few months. Surety bonds are available today; self-insurance is an option.

Mr. TAUZIN. We have been told that these new lines of insurance may not want to cover certainshippers who do not have financial assets adequate enough to justify coverage. Have you received similar comments or concerns?

Mr. SHEEHAN. We have talked to the surety companies and they have said that they are indeed going to be available. They will look at fleets in terms of their total makeup and in terms of their assets. They said that there may be some fleets, which due to their total net worth as well as their operational record, they will choose not to provide bonds for.

Mr. TAUZIN. Not to cover them. What will happen to those fleets who could be turned down by the sureties and by the new lines of insurance?

Mr. SHEEHAN. I think that with the marketplace, with the surety bond companies and the two insurers, that they are going to have to make a judgment when they come to buy insurance whether or not they are going to be covered. And if I were a——

Mr. TAUZIN. What happens to a fleet that can't get this insurance?

Mr. SHEEHAN. They will have to trade somewhere else.

Mr. TAUZIN. They can't come to America.

Mr. SHEEHAN. That is correct. If they can't provide——

Mr. TAUZIN. Therefore, these rules are likely going to limit somewhat the number of fleets that come to America. Is that right?

Mr. SHEEHAN. They may.

Mr. TAUZIN. Have you calculated in your economic analysis the costs to the American consumer of limiting the choice of shipments and the volume of fleets available to deliver supplies to America?

Mr. SHEEHAN. No, we haven't.

Mr. TAUZIN. You haven't calculated that at all!

Mr. SHEEHAN. We don't believe that that is a calculation which can be done at this point in time, sir.

Mr. TAUZIN. The reason I ask this, Mr. Sheehan, is that we received concerns and comments from some folks that we could see as high as 50 percent of the current oil supplied to the U.S. get shifted from current vessel operators to only those qualified under this rule. That is a mighty big shift if that actually occurs.

Have you received any comments or concerns that it could be as high as that level?

Mr. SHEEHAN. In the docket we received a number of comments that said if there were no alternatives available, this might be the end result.

Mr. TAUZIN. What would be the result of a 50 percent shift in oil supplied from vessels currently serving the United States ports to the remaining qualified vessels?

What is the effect of that on deliverability, security, and price in terms of shipments?

Have you not looked at that at all?

Mr. SHEEHAN. We have looked at the issue of the oil companies' fleet mix versus the independent mix. We have been told in the meetings, where API sat with the Secretary of Transportation, that the oil companies would be able to self-insure. They currently provide about 23 percent, as we understand it, of the oil that comes in.

We also understand that under the self-insurance route that they could extend that to vessels that they bareboat chartered. That would be one means of doing it. We do not rule out the possibility and we anticipate that the other lines of coverage, surety bonds, the alternate insurers and we think that there may be other insurers that come forward to fill in this gap. We do not believe that there is going to be a 50 percent reduction or shift in trade.

Mr. TAUZIN. Mr. Sheehan, you don't believe it. I hope you are right.

Mr. SHEEHAN. So do I, sir.

Mr. TAUZIN. But I have heard from folks who say that is a distinct possibility. I am asking once again, recognizing that there are people who believe that possibility whether they are right or wrong, have you done an analysis of what kind of effect would a 50 percent shift in the oil supply delivered to America from fleets no longer qualified to only fleets that would meet your new qualifications have?

Mr. SHEEHAN. No, sir, we have not done that analysis.

Mr. TAUZIN. So we have no idea what that effect could be on consumers or on the supply of oil to America? You have no idea?

Mr. SHEEHAN. We have not done that analysis.

Mr. TAUZIN. If you are right, everything is OK. If you are wrong, you don't know and cannot predict the effects and have not tried to do so.

Mr. SHEEHAN. That is correct.

Mr. TAUZIN. I am going to come back for another round.

I want to give Members a chance. I yield to Mr. Coble.

Mr. COBLE. Thank you, Mr. Chairman.

Let me put these questions to you generally and anyone can respond.

The United States never became a party to the international oil spill protocol, as you will recall, through no fault of the House. That proposal encountered shoal waters in the other body, you may remember.

Would the Coast Guard support the United States ratifying these protocols in case that ever came to light?

Admiral KRAMEK. Mr. Coble, when this was an issue back several years ago, the Coast Guard did support international standards, international ratification of the protocols, and the liability limit which I think was about $250 million or so at that particular time, and it was our recommendation that that protocol be accepted. However, that was not the protocol accepted by the Congress at that time.

Mr. COBLE. And that remains your position, I presume?

Admiral KRAMEK. Our position now is as an agent of the Administration to mete out the OPA 90 rule, mete out the law and to come up with a rule which will best fulfill the requirements that OPA 90 tasks this Nation to do. So we came up with a rule that will best meet that.

I don't have a position whether we should go to the international protocols at this time.

Mr. COBLE. Gentlemen, we may get into this subsequently as the day advances, but have you all at the Coast Guard been—for want of a better word—convinced or been the recipient of evidence that Shoreline will have the capital reserves to respond to a major oil spill or for that matter, possibly multiple oil spills in a limited amount of time?

Mr. SHEEHAN. Thank you, Mr. Coble. That is part of the approval process. When Shoreline and the other insurance entities come forward with portfolios, that will be in their financial statements, and that will be one of the criteria by which we will judge the acceptability of those entities, sir.

Mr. COBLE. Well, do you know now, Mr. Sheehan, I mean, can you tell me today whether you have been given that evidence?

Mr. SHEEHAN. I have not been provided that evidence. Shoreline came to us in December of 1993, and indicated in conceptual terms the structure and outline of a company, as well as a financial arrangement, and asked us if we could approve this conceptually. We said conceptually we could, however, at the end of the day, it would have to be determined on their capitalization, on the amount of risk that they were willing to retain on their reinsurance contracts, on the degree of supervision that they would be given by the insurance entity where they were chartered, as well as the appointment of a U.S. agent, so they have not come forward with all of those specifics on which we would need to make a determination.

Mr. COBLE. Let me put another question to you involving Shoreline, and we may get to that when the Shoreline representative is here. I have been advised—and I don't recall my source, but somewhere along the line I read or heard that Shoreline plans to per-

haps insure vessels on a per voyage basis. I guess my question is twofold: is this true to your knowledge?

And if so, what sort of financial burden would that impose upon the Coast Guard? I mean, this sort of a piecemeal operation, is that going to require more manpower, Admiral, for you all to be sure that compliance is satisfied, et cetera?

Admiral KRAMEK. We don't think that would be any more work for us if they did that, sir—changing vessels for insurance on a per voyage basis.

Mr. COBLE. Is my first premise accurate? Have you all been advised that there may be a per voyage approach?

Admiral KRAMEK. We have heard that as one of the proposals, but again we have not received any formal proposal to evaluate at this time. I had been told that we would receive it during the month of August and we are waiting for a proposal now so that we can evaluate it.

Mr. COBLE. If that is the case, you anticipate no difficulty as far as your end is concerned?

Admiral KRAMEK. Not with the paucity of information that I have been given so far.

Mr. COBLE. This question extends, Mr. Chairman, your line of questioning. And gentlemen, this is a hypothetical, but I think it can be a crucial hypothetical. What will the Coast Guard do if the majority of oil vessel owners are unable to secure or afford a guarantor by December? That is a loaded question, I will admit.

Admiral KRAMEK. That is the $64,000 question, and we will respond to that.

Mr. COBLE. Does anyone have an answer to that because, gentlemen, and Mr. Sheehan, I am not throwing daggers at you all, but this question, folks, as my late grandma used to say, makes my coffee taste bad in the morning when I think about the bad answer to this, so I would be happy to hear from you.

Mr. SHEEHAN. Sir, we have no intention of shutting down the economy of the United States. We have a number of administrative enforcement procedures that we could go through, including and up to suspension of the rule. We don't anticipate the need to do that. That is one of the options that we have available to us. Selective enforcement is another.

I think one thing that is important to note is that all of the tankers that trade in the U.S., while the deadline is the 28th of December, they all are not going to be here on the 28th of December or within that window, so there is a much smaller population that we are really talking about in that period of time.

But we will have, I am sure, some advance warning about the availability of the other insurance entities and about the self-insurance provisions. And we do have tools within our tool kit to handle that possibility.

Mr. COBLE. Thank you, Mr. Sheehan. I don't mean to be portraying the role of pessimist with this question, but the Chairman and I just went through an arduous time as a result of the Amtrak collision with a bridge that you figured would never happen, but these things have a way of happening.

I thank you, Mr. Chairman.

Mr. TAUZIN. Will the gentleman yield?

Mr. Sheehan, you mentioned selective enforcement. What is that exactly?

Mr. SHEEHAN. One of the things that occurs on an almost daily basis with us with respect to the current certificates of financial responsibility that we issue is that we receive binders. Very often it is at the last minute for a vessel, which is either in-bound or to be in the U.S. port within a short period of time. While they don't meet the absolute letter of the law by having the appropriate certificate on board, we accept those binders as proof that they have engaged in the guaranty process and so we will let them come in without the actual valid certificate, but with the assurance of the guarantor that they have provided coverage. So, we would not hold them up for a technicality as long as the underlying insurance was there.

Mr. TAUZIN. I want to come back to that.

I thank the gentleman for yielding. The gentleman from Virginia, Mr. Pickett, for questions.

Mr. PICKETT. Thank you, Mr. Chairman. Will the effect of these rules be to give any kind of preferable treatment to foreign carriers as opposed to U.S. carriers?

Mr. SHEEHAN. No, sir.

Mr. PICKETT. And what kind of procedures are going to be used to ensure that foreign carriers coming into U.S. ports are going to be in compliance with these rules?

Mr. SHEEHAN. Foreign carriers, their owners and operators will have to apply for a certificate of financial responsibility. There is a form which is required to do that. The Coast Guard then issues a document to those owners and operators which is carried on board that vessel. We have enforcement personnel located throughout the United States who when we receive notification that a ship is in-bound, pull it up on our marine safety information system and look at the status of the certificate of financial responsibility. Is it valid? Is it invalid? Is it issued to the current operator?

If it is not valid, we have two options. We can deny entry. Normally what is done is we will then contact that owner and operator, and perhaps it has been a problem with their guarantor. The guarantor, to alleviate that problem, can come to us and give us a binder. But we have a routine where we board these ships today to make sure that this law is adequately enforced. We have had a number of detentions

Mr. PICKETT. The companies that you have made reference to here, that I think you said the two companies and I saw them listed somewhere in the materials here, what kind of investigation and what kind of procedures do you have to ensure that they will be financially solvent and able to meet all the commitments that they may be insuring?

Mr. SHEEHAN. We have, over the past 20 years as part of the certificate of financial responsibility program, routinely examined, approved and rejected insurers. We go through a number of tests of these insurers. We look at their net worth.

We make sure that the net worth or after-capitalization is sufficient to cover a potential loss. We look at the amount of risk that they retain. We look at the amount of risk that they reinsure. We look at their reinsurance arrangements.

We also make sure that they have oversight in the area in which they are chartered. We also make sure that they have a U.S. agent for process. If it were a U.S. insurer, we would look to the A.M. Best Company rating system, which is a standard industry-wide methodology of examining the viability of insurance companies.

Mr. PICKETT. I notice here that one of these companies, for example, that is referred to, it states that it is incorporated in Bermuda, and I understand there are some very creative accounting procedures that may be followed by some of the offshore insurance companies. What do you do about those kinds of situations?

Mr. SHEEHAN. Bermuda does have a recognized and legitimate insurance authority which oversees the general operation of insurers. We currently have a number of insurers that are currently based in Bermuda and we have had good experience with those, including P&I clubs.

Mr. PICKETT. Picking up on the final question, and deep concern that I have is implicit in some of the other questions that were asked, but what we have done by the law and now the regulations that are being established is to create a situation where only the very large companies, the very large oil companies, are going to be able to participate in this market and that pricing of products will be at the discretion of these very few very large companies?

Mr. SHEEHAN. The pricing of the insurance surely is going to be at the discretion of the insurance companies in terms of premiums.

Mr. PICKETT. Excuse me, I am speaking of carriers, the petroleum carriers themselves. Have we set up a situation where only—very large oil companies with large resources will be the only ones with access to the market and, therefore, they will be able to dictate what prices are going to be?

Mr. SHEEHAN. I don't believe that is the case, sir.

Mr. PICKETT. Well, can you expand on that a little bit? If we have all of these heavy financial requirements and only the very financially strong and powerful companies are going to be able to qualify, how can it be otherwise?

Mr. SHEEHAN. If you need to provide a coverage upon which we issue a certificate of financial responsibility, that becomes a business cost that is spread across the entire tanker industry. That is going to be a cost. There is no doubt about that. It is going to be more than what they are currently paying.

Those that self-insure and have the ability to self-insure are genuinely going to have a slight advantage over someone who cannot. However, these costs are ones which, in our view, and I think, as we had stated in the final rule as well as in the Regulatory Impact Analysis, these costs are ones which in our view are still under the control of the ship owner.

If the P&I Clubs, and I think you will be hearing from them today, but if the ship owners, which are the P&I Clubs, direct their P&I Clubs to provide coverage, then you will be back on an absolutely level playing field. So it is in many ways a situation which is somewhat self-generating. You will hear, I think, probably some testimony this afternoon which says, no, we can't do that. But I would submit, sir, that one of the organizations which is here and going to testify is indeed a P&I club. We have another P&I club called Ocean Marine, which is going to write dry cargo coverage,

so it doesn't share the same concerns that the rest of the clubs do. So there doesn't appear to be total unanimity with respect to the Clubs' position.

Mr. PICKETT. The part that concerns me a bit is this issue about the availability of insurance to the smaller or less financially stable companies and the parallel in my mind is that of the risk that is associated with the writing of bonds for construction purposes, that this has gotten to be quite a high-risk business and it has come to the point that in many cases there are only a very few companies that can get a responsible insurance company to write a bond for them. Is that where we are headed in this business with the bonding of the oil transporters?

Mr. SHEEHAN. I don't believe that that is the case. I would expand a bit on my previous answer.

If you are also addressing the inland, the barge industry, which is a large component of this particular industry, that delivers petroleum, we have had no indication that the Water Quality Insurance Syndicate, which currently provides guaranties upon which we issue certificates of financial responsibility, we have had no indication that they are not going to continue that practice.

And, indeed, I have talked to their representatives and as far as I am led to understand, they are going to be able to continue to provide that. And indeed, they can expand their marketplace to provide coverage to a wider group in the tank-barge industry than is currently served today.

Mr. PICKETT. Thank you, Mr. Chairman.

Mr. TAUZIN. Thank you, Mr. Pickett.

The gentleman from Virginia, Mr. Bateman is recognized.

Mr. BATEMAN. Thank you, Mr. Chairman. I have very few questions, frankly, because I have not had the opportunity to go through the material that is here before me. I want to comment, though, that I have listened with very grave trepidation about where we are and where we appear to be heading.

I have not been one of the great fans of our oil spill liability solution. I think from the beginning it has been fraught with the likelihood that we wanted to feel good and sort of a "wouldn't it be nice" approach that too often ignored the realities of the actual world of commerce and the marketplace.

What I am hearing today seems to reinforce, frankly, those concerns. I find it very disconcerting that we are embarked on something where we are dealing with wonderful concepts, but without any confidence that they are rooted in any reality. And concepts are nice, but not when they defy reality.

To sit here and to hear it said that there is no defense to someone who is insured or guaranteed of losses from some liability occurrence, even though they haven't paid a premium, just defies any logic. How do you possibly get anyone to accept that kind of a risk if they are not even assured of getting paid whatever premium or fee was supposed to be the commitment? Why would anybody undertake to do anything if we are going to do such things as that?

I can assure you, Mr. Chairman, that you more than tweaked my interest, and I will be visiting this issue and will want to discuss it with you and my colleagues on the committee, but I can't tell you

that I have heard anything that was much more disquieting than what I have been hearing this morning.

Mr. TAUZIN. Thank you, Mr. Chairman Bateman.

The gentleman from North Carolina, Mr. Lancaster.

Mr. LANCASTER. Thank you, Mr. Chairman. I would like to know a little bit more about how self-insurance will work. Will it be possible for a major to simply show assets of an amount that is satisfactory to you or will it be necessary for those assets to be in some way segregated by trust or other instrument so that they will be available only for purposes of the guarantee?

Mr. SHEEHAN. Thank you, sir.

The self-insurance is a component which we currently use in the certificate of financial responsibility program. It is one which you basically take a look at the size of the largest vessel in the fleet that you need to insure. There are two tests for it.

You basically take a look, an accounting of your U.S. assets; and you subtract your worldwide liabilities. You then subject it to a working capital test, which is basically your U.S. short-term assets less short-term worldwide liabilities. You don't have to set it aside.

The working capital provision is one which we nominally use to make sure that there is adequate flexibility and adequate liquidity but we recognize, sir, that there are quite a number of companies which are sometimes fully invested in long-term securities. They do not have a lot of cash sitting around, and they do not have it in trusts. We have provided within the rulemaking itself a provision to waive that. It is not an automatic waiver, but we have done it in the past and it takes into account the overall financial stability of the company. We have a series of marine examiners who have been doing this for a number of years who look at this.

Mr. LANCASTER. Is this guarantee in some way filed under the uniform codes of commercial—UCC in some way that it then becomes a lien? Or is it possible for those assets to be encumbered subsequent to the giving of the guarantee so that at the time the guarantee is called, those assets are not available for the purposes for which it was given?

Mr. SHEEHAN. I don't believe it is filed as a lien. And I will check with my counsel. I don't believe that we do that. On some companies we require a six-month financial accounting to make sure that that situation doesn't occur.

Mr. LANCASTER. Would it be possible for companies to give guarantees for third-party carriers or will it be only if they are a certified guarantor?

Mr. SHEEHAN. No, sir, they could provide coverage for third-party carriers. I have been approached by one company who is interested in doing that already. They would basically have to meet the self-insurance tests, but that would be an option for them to do.

Mr. LANCASTER. It would not be the same test that you would require of guarantors, but would be the same test that you now require of self-insurers.

Mr. SHEEHAN. That is correct, sir.

Mr. LANCASTER. Is that a significant source, you think, of guarantees that might be used for third-party carriers?

Mr. SHEEHAN. I don't know. It is a possibility.

As I indicated, I had a visit the other day from a company that had indicated they wanted to explore this because they were looking at it a constructive way, how to comply with this and how to provide coverage to some of their third-party carriers. I am not sure at the end of the day what the mix is going to be in terms of self-insurance, surety bond coverage, straightforward insurers. It is too soon to tell.

Mr. LANCASTER. I share the incredulity of the Chairman and Mr. Bateman with regard to the defense or lack of a defense for nonpayment of premium. And so there must be an explanation that we are missing as to why that is in place.

Is it simply anticipated that everybody will prepay and that before they undertake any shipment that full premium will be paid for the guarantee and that there will not be any basis on which, as in all other commercial instances, there are installment payments spread out over the course of a year?

Mr. SHEEHAN. With respect to surety bonds, those are prepaid. With respect to some of the insurance entities which are being examined or will be shortly, I understand that at least one is going to require prepayment.

I think that the matter really hinges on the difference between, as Mr. Horowitz pointed out, standard insurance coverage and a guaranty. They are different entities. And if you are going to have a guaranty, it has to have some ironclad provision for it.

Now, when we receive notification of cancellation of a policy—for example non-payment of premium—we will then cancel the certificate of financial responsibility, which means that that ship will not be able to trade. They are not on the hook forever is I think the key point. In today's system, when they haven't received payment for a premium, they, in turn, notify us. We in turn then cancel the certificate of financial responsibility.

Mr. LANCASTER. There are other guarantee instruments which are being used as a model here for which nonpayment is not given or not allowed as a defense?

Mr. SHEEHAN. I believe that under the international regime, which was spoken of earlier. Under the TAPS regime, as well as the Outer Continental Lands Shelf Act, which is in effect, that nonpayment is not able to be used as a defense.

Mr. LANCASTER. Thank you very much.

Mr. TAUZIN. Thank you, Mr. Lancaster. The gentleman from Maryland, is recognized.

Thank you, Mr. Gilchrest.

The gentleman from Mississippi, Mr. Taylor, is recognized.

Mr. TAYLOR. Thank you, Mr. Chairman. And I want to thank you for holding this hearing and for the staff putting together a really excellent briefing. I want to open this up to the panel.

I have been trying without much success for a few months to interest the tanker community trying to go to double hulls voluntarily, and one of the ways that I have tried to do that is I have said what if we limited liability for people who voluntarily went to double hulls with the idea that it is better to prevent a spill than to beat somebody over the head after a spill.

And I have had two interesting responses, one from the environmental community and one from the tanker owners and operators.

The environmental community doesn't want to reopen OPA 90 because they think there is unlimited liability and that they will be able to beat somebody over the head and the threat of that will prevent a spill.

Interestingly enough, tanker owners and operators don't have any interest in limited liability and reducing that. They seem to have no interest in going to double hulls even if we limited their liability. And I find that very interesting.

Now I heard talk, and I have nothing to back this up other than talk that they have figured out a way to beat OPA 90 by chartering offshore dummy corporations and therefore they have limited their liability because when the Coast Guard goes to collect, there is just a piece of paper somewhere and you can't collect money from a piece of paper. Interestingly enough, then the environmental community is really out of luck because you cannot get unlimited liability from a dummy corporation.

I wish the panel would respond to that, because I am hearing this too often for there not to be some fire underneath that smoke.

Mr. SHEEHAN. Mr. Taylor, I think that you have certainly focused in on the genuine purpose of what the certificate of financial responsibility is for.

It is for exactly that instance when the ship owner—and the majority of them don't—but when the ship owner decides to take a walk away from his responsibilities that there be some surety of payment and surety of payment to claimants. The way that that is done is through the certificate of financial responsibility program.

Mr. TAYLOR. How would you explain, sir, and I am taking this strictly from the staff bulletin, so—anyway, on page 2 and 3 of the staff bulletin and particularly on page 3, any vessel navigating without a COFR in waters covered by OPA 90 may be denied entry.

Well, if they may be denied entry, obviously they don't have to have a COFR even though page 2 would lead me to believe that they had to have one.

Mr. SHEEHAN. We may deny entry.

We take a look on all vessels that come to U.S. ports to see if they have a certificate of financial responsibility. One of the things that frequently happens is that enroute, either the operator will change, and if that is indeed a paper type of transfer of an operator from one name to another name, that by virtue of doing that, you invalidate that certificate of financial responsibility.

When we find that out, we query our information system and see that that has happened, we will then contact the operator. They in turn will then contact the guarantor to make sure that they actually do have coverage and that we are notified. So in those rare instances where they don't have a valid certificate, where their guarantor does not give us a binder, where there is no connection, we do deny entry to that ship. In some instances, we end up with situation where we detain a ship.

Mr. TAYLOR. But, again, going back to this first paragraph top of page 3, it says "may", not "shall". Does that mean some of them get in?

Mr. SHEEHAN. I don't believe so, sir.

Mr. TAYLOR. Then why does it say "may"?

Mr. SHEEHAN. Because it is the transitional situation with respect to the issuance of the underlying guaranties. Sometimes we end up with a situation where they have applied for a certificate of financial responsibility, we have mailed it to the operator and it hasn't arrived there yet, so they indeed have a valid one but it is not on board. And so in those particular instances, that valid one, according to the regulations, is not on board we would, in fact, let them in.

Mr. TAYLOR. Could a vessel carrying chemicals, oil or other hazardous substances over 300 gross tons enter this country without a certificate of financial responsibility, carrying these things as cargo and not as fuel?

Mr. SHEEHAN. The possibility exists that could happen. We have a very active enforcement mechanism to take steps that it does not happen. We have linked up in the past two years with our Office of Marine Safety to make sure that our port inspectors and indeed the U.S. Customs, which plays a role in this as well, have current information. Our number of detentions and enforcements have gone up rather drastically.

There could be a ship which slips in which has not given a port notification, for example, and that is a situation which could occur. You could have a ship which we didn't see. Our people didn't know about and Customs didn't know about.

Mr. TAYLOR. If you would please explain why you used word "may" instead of "shall." I always thought of that as sort of arbitrary enforcement; we will enforce for you, but not for you.

Mr. SHEEHAN. My counsel just advised me that those are the words which are in OPA 90 itself, that we may deny entry.

Mr. TAYLOR. Well, does that need to be changed?

Mr. SHEEHAN. I think it probably provides, with the enforcement regime that we have in place, the appropriate flexibility. There is a requirement that they have these certificates. This is an enforcement tool.

The denial of entry is an enforcement tool. There are other enforcement tools such as civil penalties and the ultimate enforcement tool is, I believe, seizure of the vessel.

Mr. TAYLOR. Getting back to the offshore corporations, how do you enforce that?

Mr. SHEEHAN. Through the underlying guaranties upon which we base the certificate of financial responsibility. In other words, that is one of the reasons that we have a direct tie and a direct—the ability to have direct action and direct agreement with the insurer between the United States Government and that insurer, exclusive of the particular operator. And that is the mechanism. It has worked in concept for——

Mr. TAYLOR. And all of these insurers are United States corporations?

Mr. SHEEHAN. No, sir, many of them are foreign corporations. Many of them are currently P&I Clubs, Lloyd's of London, there are a variety of guarantors.

Mr. TAYLOR. Do you have a list of approved insurers.

Mr. SHEEHAN. Yes, sir.

Mr. TAYLOR. And it has to be one of those groups and you are telling me that you have a mechanism to collect from every one of these insurers should the worst happen?

Mr. SHEEHAN. Yes, we do, and I think to the credit of the insurance industry and certainly to the credit of the P&I Clubs, they have stepped forward in 99.9 percent of the cases and come forward willingly to the claimant. They have come forward to pay for removal costs so we have not had to exercise that particular provision except in probably less than 10 instances over the last 20-some odd years.

Mr. TAYLOR. Just one last question and I will put it up to the panel. I have noticed that you pay the same fine whether you have the single hull and you wait to the last day to go to the double hull or if you have a double hull. Since previous testimony before the committee said that something like 95 percent of all the spills that occurred in this country could have been prevented with I double hull, wouldn't it make sense to give people a financial incentive to go to double hulls, just as smokers get a break on their health insurance and people with fire alarms get a break on their homeowners insurance? If you can prevent a problem, it would make a heck of a lot more sense than trying to clean it up afterwards.

Mr. SHEEHAN. I, sir, have been a long-term proponent of double hulls. I think that the concept is superb. I think that the high levels of liability within OPA 90 also serve as a great incentive. I think that if you were a shipowner, I would want to have a double hull to ultimately limit the potential of my liability. I am not sure how we would craft something like that. I know it is an interesting concept.

Admiral KRAMEK. I think it is an insurance company issue, too. How safe you are should be determined by the industry as to how much your premiums should be. And in marine safety circles, we have talked about that for years. I would assume that people who have safer operations would have less of a cost of insurance for any risks that they may be taking. That doesn't particularly affect this rule, but it certainly can be debated.

Mr. TAYLOR. Does the Coast Guard have the authority to do that under the present?

Admiral KRAMEK. No, we don't have any authority to do that under the present law.

Mr. TAYLOR. Thank you, Mr. Chairman.

Mr. TAUZIN. Thank you, Mr. Taylor.

Gentlemen. Mr. Sheehan, in particular, you assert that there is a distinction between a guarantee and an insurance company; right? Is that why you haven't allowed the policy defense for nonpayment of premium?

Mr. SHEEHAN. My assertion is that there is a difference between an insurance policy and a guaranty, yes, sir.

Mr. TAUZIN. That distinction, as I take it, was also recognized by Congress, and I want to read you the statute precisely. It said: Financial responsibility under this section may be established by any one or by any combination of the following methods which the Secretary or the President determines to be acceptable. And then Congress lists the various forms of commercial indemnity. Congress listed: evidence of insurance, surety bond, guarantee, letter of cred-

it, qualification as a self-insurer or other evidence of financial responsibility. Obviously, Congress agreed with you that there is a distinction between guarantees and insurance policies.

Do you have any quarrel with that?

Mr. SHEEHAN. No, sir.

Mr. TAUZIN. Given that there is a distinction between guarantees and insurance policies and, in fact, between them, and other evidence like letters of credit and surety bonds, why did you in these regulations choose to equate insurance coverage with guarantees in providing the direct action requirement against insurance policies as against guarantors?

The direct action requirement is found in the next section which says that claims against guarantors—that claims with liability may be established, may be asserted directly against the guarantor. In your regulations, you have—you tell me that you have recognized the distinction between these forms of indemnity, and yet, you then take the next section which requires direct action and you apply it across the board to all of these forms of indemnity when the Congress clearly provided for direct action against guarantors without mention of insurance policies, surety bonds or letters of credit.

By what authority have you made this decision under your regulations?

Mr. SHEEHAN. I believe it is contained in the definition of what a guarantor is. The insurance policy is the basis upon which a guaranty is provided and the guarantor is the individual or person, as I believe it is defined in the law, that provides the evidence upon which we issue a certificate of financial responsibility. So we then have an agreement between the guarantor and the U.S. Government and that guarantor then is subject to direct action.

Mr. TAUZIN. Even though the guarantor in this case is an insurance company who has issued an insurance policy, you are now equating them for the purposes in terms of direct action, when you indicated they were not the same when it came to policy defenses?

Mr. SHEEHAN. The insurance guaranty is the evidence that they come forward with and we then enter into an agreement with writer of that insurance guaranty.

Mr. TAUZIN. You follow my point?

Mr. SHEEHAN. I follow your point, but there is a distinction.

Mr. TAUZIN. You have argued persuasively that guarantors are not insurance companies or necessarily insurance policies. For that reason, the normal defense to an insurance policy that you haven't paid the premium, is not available to the guarantors, but then on the same issue, you tell me that they are the same under the act when it comes for direct action requirements.

Mr. SHEEHAN. In our view, I believe that if the law had been written that you simply had to provide an insurance policy and not have the concept of a guarantor, which issues a guaranty and provides a guaranty, that would be different.

Mr. TAUZIN. But that is what the law precisely said. It says any of the following methods or any combination of those following methods, and then it lists the very distinct forms of indemnity, evidence of insurance, surety bond, guarantees.

You are telling me that if the law had allowed these different forms, that you would not necessarily have to equate them. I am

reading you the language that clearly authorizes these different forms or any combination of them, guarantees are listed as a specific, separate entity from evidence of insurance, surety bond, letters of credit and other evidence said, please explain.

Mr. SHEEHAN. Yes, sir, all of those categories, insurers, surety bonds, folks who provide financial guaranties, are indeed guarantors under the definition that is contained in OPA 90. Guarantor means any person other than the responsible party who provides evidence of financial responsibility for a responsible party under this act.

We spoke earlier about the opportunity for individuals to provide coverage under the financial guaranty portion of this law to third parties, that is an option. They would, indeed, be called guarantors as well. So you would have a guarantor that provided the financial guaranty under the self-insurance rules. In other words——

Mr. TAUZIN. Help me out. What is the difference in Section E between a guarantee and a guarantor who provides evidence of insurance? Why did Congress have these two listings if there wasn't a difference, please tell me.

Mr. SHEEHAN. I think it is a different mechanism. It is a different financial way of addressing the guarantor problem.

Mr. TAUZIN. What is a guarantee, please? When Congress used the term "guarantee" in Section E, what do you think the Congress meant? As opposed to evidence of insurance? Did it mean anything? Congress just erred when it listed them separately.

Mr. SHEEHAN. It was a mechanism which was in the previous 311 law. It was simply, I think included again. It is a different financial way of addressing the issue upon which you issue a certificate of financial responsibility.

Mr. TAUZIN. But then you apply all the same commercial rules to these different forms. Let me be specific. Section E indicates that the Secretary or the President as appropriate may specify policy or other contractual terms, conditions or defenses—or defenses which are necessary or which are unacceptable. So it leaves to the President and the Secretary broad discretion in defining the availability of defenses.

Section F indicates that in defending against a claim that the guarantor—I assume you say those are insurance companies who issued policies of insurance—the guarantor may invoke any defense authorized under Section E. I read that to say that any defense the Secretary and the President find are necessary, which are unacceptable in that broad discretion.

Policy defenses normally include nonpayment of premiums. Obviously, under Section E you have the right to say that would be true for insurance policies which serve as the underlying instruments by which guarantors satisfy the statute. Obviously, under Section F, guarantors may invoke those defenses.

Why did you choose not to make them available if insurance forms are, in fact, as indicated under Section E, separate and distinct categories of indemnities which are authorized under the act?

Mr. SHEEHAN. We took a hard look at this.

Mr. TAUZIN. We are, too.

Mr. SHEEHAN. Yes, sir, and I appreciate that, and I appreciate the opportunity to explain our rationale for doing it.

Mr. TAUZIN. Please do, sir.

Mr. SHEEHAN. Our rationale is that if a guaranty is to mean something, it is to mean something different than the underlying policy, that there is a certainty of funding other than a promise to pay. If you include the myriad of policy defenses which you provided normally under P&I Club coverage, for example, that surety does not exist. And our view was that in order to make the surety for the American public there, that we were only going to permit those defenses permitted by law and the additional ones——

Mr. TAUZIN. Sir, by doing this you have literally equated two terms that were at least listed separately by Congress as authorized acceptable forms of indemnity. You have equated them. You have said that insurance company policies like P&I coverage will be the same as guarantees even though they are listed separately under the act.

Mr. SHEEHAN. They are different entities—the insurance guarantor and the financial guarantor under different financial tests.

Mr. TAUZIN. But you apply the same defense rule to them. This is our concern, sir. Let me put it very simply. The concern is that by redefining the terms of the insurance policy to exclude defenses normally available to the insurance policy, you have effectively required that those insurance policies now be guarantees without those defenses. And you may have excluded from the marketplace P&I coverage, except as reinsurers. That is what you have done.

What you have done for us is layered coverage. You have literally built a new niche for some new insurance companies to be formed, which, in order to cover all the shippers that are going to need coverage, may in fact end up depending upon the P&I Clubs to be reinsurers. As Lloyd's of London has now done behind the P&I Clubs.

So now we will have three layers instead of two. We will have new insurance companies who may qualify. We don't know whether they will or not, who may offer coverage for everyone or who may not. However, in order to cover everyone, it may require P&I reinsurance with Lloyd's of London behind all of that. We will have so many layers, and I assume extra layers of profit involved, too. Rather than changing the security of coverage for Americans under OPA 90, all we will have done was to add another layer and increase costs with no real security larger than what we have today under P&I coverage.

If that is the effect of these OPA 90 regulations, we in the end-run would have just created some new companies out there to make some new profits because our Coast Guard created this niche for them. And, the P&I Clubs can only play by reinsuring these companies. In the long run, we will have just increased the cost to consumers with no real extra security for payment of claims under oil spills.

Now, if my scenario of my concern is correct, why would our Coast Guard want to be a party to that kind of a scenario?

Mr. SHEEHAN. I would respond in this way: we looked at, and we put on several sets of glasses, if you will, when we looked at the proposal which has been put forward by many facets of the industry to use P&I coverage as an asset. I think that we have explained in our rulemaking——

Mr. TAUZIN. I have that explanation before me.

Mr. SHEEHAN. One of the unique results that would occur if we accepted that, if we found a legal way to accept that premise that they were an asset, one of the effects would be that right now we have 68 percent of the coverage for COFRs in the U.S. are done by P&I Clubs, and about the remaining—except about 3 percent—97 percent is done by insurers and P&I Clubs. If we accepted those as the basis upon which we gave a self-insurance test and said that would be—they would then be issued certificates of financial responsibility, the U.S. Government and the U.S. consumer would end up in an inferior position after the passage of OPA 90 than it was prior to the passage of OPA 90, because prior to passage of OPA 90, we had direct action against that band of 97 percent that provided coverage.

If we accept the self-insurance test by including P&I Clubs and insurance industry as an asset, we have no direct action, so we have reversed the impact of the Oil Pollution Act. And so I think in terms of surety of payment, Mr. Chairman, we would be going in the other direction.

Mr. TAUZIN. But we have changed what is possible to claim under this insurance coverage dramatically under OPA 90. We have added natural resource damage, third-party claims, all kinds of other new claims to be filed against the body of insurance that provided coverage for Americans under the current regime.

And now, by redefining this insurance coverage as this category of guarantors without normal defenses available to them, we may have excluded that coverage from the marketplace and created the scenario that I provided to you where we have new layers, without the extra coverage and protection to the consumers.

I am distressed by the fact that you folks never even put the pencil to what might happen if 50 percent of the oil supplies can't travel anymore on vessels that can't get COFRs under your new regime. Particularly, if that sort of thing happens and the only consolation that you will give us is that you will accept binders, or suspend the regulations. How can you feel comfortable today before this committee and before the American public saying that you served us well by excluding the very terms of your direct action and your lack of policy defenses, the most important security coverage we now have today in the P&I coverage?

Mr. SHEEHAN. Mr. Chairman, we haven't excluded them. That is not our choice to exclude.

Mr. TAUZIN. If you write terms by which they can't play, you have excluded them.

Mr. SHEEHAN. They have made that decision themselves.

Mr. TAUZIN. They have made the decision that the terms are going to be terms they can't play under? I don't buy that argument.

You are making the rules here. They are going to have to live by them or not, and they are saying that they can't live by them. They are telling us all that.

The reality is that your answer for us is that some new forms of insurance are coming, not to worry. What we are also told is that these new forms of insurance may, in fact, need the P&I Clubs as reinsurers to be sustainable for the great body of shippers. And we need them. We are getting some mighty different signals here in

a very short timeframe for this Nation to feel comfortable that these rules are going to work well.

I am reading here some very, very distressful concerns by shippers who are going to have to play under these rules. They are not writing the rules. We are—you are, not them.

Mr. SHEEHAN. Yes, sir.

Mr. TAUZIN. When you talk about selective enforcement, and if all this happens as some are predicting—if, in fact, the barge does hit the bridge and because we wanted to feel good and make a few States and the environmental community believe we have done something great for them—if all of that happens, and a great majority of these shippers cannot even produce these binders for you, which obviously means they are going to get insurance, instead, they show up at the border with oil shipments critical for folks in Boston who need fuel oil in the middle of the winter, the Coast Guard has to say you don't have a binder, your P&I coverage isn't any good, and I understand the new forms of insurance have not accepted you, therefore you have to turn around. What is your answer to those folks in Boston who need fuel oil that day when it can't be delivered?

Mr. SHEEHAN. As I indicated before, I don't think that is going to happen.

Mr. TAUZIN. You don't think it is going to happen. So, we should all go to sleep feeling good tonight?

Mr. SHEEHAN. No, sir, I don't think that is the case at all. I think that we have attempted to put forward a regulation which comports with the requirements in OPA 90. We have had extensive discussions with the P&I Clubs.

I went back and read the full testimony that occurred in the hearings that were held before you in 1991. And I was struck, sir, by one of the questions which you asked of the P&I Clubs at the time: Do you think that the Coast Guard has the flexibility to do what some of the shipowners would like to have done? And the response was: No, I don't believe they have got the flexibility to do that, looking at the law itself.

Mr. TAUZIN. I just read you the flexibility. I read you this section that says you could have adopted a rule that allows policy defenses comparable to those of P&I Clubs operate under, and you chose not to do that.

Mr. SHEEHAN. Sir, I had discussions and we have had discussions with the P&I Clubs concerning policy defenses. If you had some policy defenses other than the full bode of policy defenses, which ones would you pick?

Mr. TAUZIN. Would you comment to the record about the ones other than all of the policy defenses that you want?

Mr. SHEEHAN. The comments that I have received, and that my staff has received, and that have been made in public fora and have been made before this committee also, our problem is not the certificate of financial responsibility rule, our problem is the Oil Pollution Act of 1990. So I have selectively gone through and said, if we were able to legislatively get rid of the third-party direct action, would that be sufficient for you to write guaranties?

Well, they answer that that is only part of the problem. I likewise have gone through the entire list of issues, and if there was

flexibility in there, I have not been able to generate it from the P&I Club community.

Mr. TAUZIN. I tell you what we have heard from them and what we are going to hear from them again today, and many times between now and December, is that, if their policy defenses were recognized and they were not necessarily subjected to the direct action as guarantors, they would qualify.

Mr. SHEEHAN. And they also indicated that if we went back to the defenses that were there under pre-OPA, which basically means that you don't have Title I of OPA. That is the conundrum that we have got.

Mr. TAUZIN. I realize that we have a statute and operate under a statute. I pointed to you flexibilities that I think are there. You have indicated that for your own reasons, you have chosen not to exercise that flexibility. This is a little unrelated, but I want to raise it to give you an idea of what we face in Congress.

We write laws that we think are good and then we see them applied in the real world, and as Mr. Bateman says, we are shocked. Just two days ago, a Boy Scout, 14 years old, was lost in a wilderness in Arizona, a wilderness we created by a Federal Act.

When the State police rescue helicopters finally located this young man who was lost in the wilderness without food, the State police helicopter requested park police permission to land. They were denied permission to land because wilderness rules require that no motorized vehicle operate in the wilderness. That young man had to survive for 24 hours lost in the wilderness because our government has written a law, when applied by the Park Service, refused permission to a State police helicopter to rescue that young man.

If the parents had treated that young man that way, they would be in prison for child abuse. But our government wrote a law implemented by our agencies without any common sense. I know that is a little unrelated to what we are doing, but it is related.

It is related, if, in fact, our worst fears are realized and you folks haven't even put a pencil to it and we are left in December with conditions whereby all we have done is left lots of shippers without coverage and a lot of American consumers dependent upon those shipments with no answers from the Coast Guard, other than we might have to suspend the regulations.

I want you to know, I can't sleep well and my coffee does not taste good if that is what I have to rely upon.

Mr. Coble.

Mr. COBLE. Well, Mr. Chairman, I will just for emphasis—purposes of emphasis only, gentlemen, before you excuse the first panel, I want Mr. Chairman, to repeat the question I asked before.

And gentlemen, I would like for you all to take this home with you, and you don't mind doing it. And that question was: What will the Coast Guard do if the majority of oil vessel owners are unable to secure or afford a guarantor by December?

My uneasiness has not been assuaged with the passage of hours that have gone on this morning, gentlemen, so the next time we see you, I hope that there will be an answer to that question that will make my coffee taste good and will make me sleep soundly at night.

If anybody wants to respond to that, that is the same question I put to you earlier.

Admiral KRAMEK. We will provide you a detailed answer with that, Mr. Coble. I can't guarantee what it will do for your coffee.

Mr. COBLE. Or my sleep.

Admiral KRAMEK. But we definitely owe you that answer and we will provide it promptly to give you all the administrative actions that will take place.

[The material submitted may be found at end of hearing.]

Mr. SHEEHAN. I spoke moments ago about the November 1991 hearing. And Mr. Coghlin, who is behind me, pointed out his exact testimony concerning one of the issues that we are discussing, the only way out we can see, and I quote this because I want to make it absolutely correct, and perhaps I misstated it, but I think in another portion of the testimony it was inferred that the problem is with OPA 90 and not with this particular rulemaking.

But with respect to how they might comply, he has said the only way out as we can see, is to use the wider pass that Congress appeared to leave available to the Coast Guard in making their regulations, such as the provisions for other evidence.

Mr. TAUZIN. Will the gentleman yield?

I want to point out that what Mr. Sheehan is telling this committee is that Mr. Coghlin did testify is that, one, the way out is for the Coast Guard to use the flexibilities provided by Congress in the very words of the act that I just cited to Mr. Sheehan.

The gentleman from Mississippi, Mr. Taylor.

Mr. TAYLOR. Thank you, Mr. Chairman.

I realize this is off the subject of certificates of financial responsibility, but it is on the subject of OPA 90. Where do our smaller, those that only handle a hundred, or possibly 1,000 or 2,000 gallons of fuel, stand with regard to their certificates of financial responsibility? What sort of insurance will they have to buy?

The question has been raised by both the U.S. and a number of other organizations. I have not heard any formal response and I was hoping that I could get something now.

Mr. SHEEHAN. That is a question I would have to defer to the Minerals Management Service. That is a rulemaking which they are proceeding with, that is not one under our cognizance.

Admiral KRAMEK. That is correct, that is not under our cognizance, sir, and we would have to get another agency to give you an answer to that.

Mr. TAYLOR. Would you?

Admiral KRAMEK. Yes, certainly will.

Mr. TAYLOR. Thank you, Mr. Chairman.

[The following was submitted:]

The Mineral Management Service, the agency that administers the offshore facility financial responsibility program, has been requested to respond directly to the Subcommittee.

The letter referred to above may be found at end of hearing.

For more information, see also hearing report Serial No. 103–79.

Mr. TAUZIN. One final thing, Admiral. Have you got that number now on the total financial impact?

Admiral KRAMEK. We will have it by the end of this hearing, sir. We will have it definitely before this hearing concludes.

Mr. TAUZIN. Thank you, Admiral. We appreciate your testimony.

And Mr. Sheehan and Mr. Horowitz, we appreciate it.

We will have some written questions that we will submit to you to complete the record here this morning.

[The questions and responses may be found at end of hearing.]

Admiral KRAMEK. Mr. Chairman, I think we have the answer to that question.

Mr. TAUZIN. We have one number in the RIA, which indicates $415 million, which seems like an awfully small sum.

Mr. SHEEHAN. That is the number——

Mr. TAUZIN. Is that what you are working with?

Thank you for your testimony. We will submit written questions to you.

If you have any other written documentation or statements that you want to make for the record, we will keep it open for a couple of weeks to do so.

Mr. SHEEHAN. Thank you for the opportunity to appear, sir.

Mr. TAUZIN. Thank you.

[The following was submitted:]

CLARIFICATION OF THE TERM "GUARANTOR" AND THE METHODS FOR DEMONSTRATING FINANCIAL RESPONSIBILITY

During the hearing there was a technical discussion concerning the relationship between an OPA "guarantor" and the methods for demonstrating financial responsibility. The following amplifying information is provided.

Congress enabled the Secretary to accept one or more methods for demonstrating financial responsibility. Specifically enumerated are: "evidence of insurance, surety bond, guarantee, letter of credit, qualification as a self-insurer, or other evidence of financial responsibility." 33 U.S.C. 2716(e). Each of these enumerated methods concerns a distinct arrangement.

All methods of financial responsibility must be "evidenced". Anyone that provides those "evidences" (including providers of "guarantees") are "guarantors".

As OPA explicitly provides, "any person, other than a responsible party, who provides evidence of financial responsibility for a responsible party under this Act [OPA]" is a "guarantor". 33 U.S.C. 2701(13). A "guarantor" is subject to direct action. 33 U.S.C. 1016(f). Congress provided no basis for the Secretary to exempt any "guarantor" from direct action. The definition of "guarantor" does not only apply to the entity providing a financial "guarantee" (i.e., a financial guarantor). Rather, Congress, by defining the term "guarantor" as it did, specified that all providers of financial responsibility, regardless of the underlying method for that evidence, are guarantors subject to direct action.

Mr. TAUZIN. While we are waiting for the second panel to take their place, I want to make clear for the record that the amount of $415 million is based upon an assumption that commercial insurers would be successful in obtaining a premium of $2.03 per gross ton per voyage. That is the assumption upon which that low number is based.

The second panel will please assemble.

We will be using the lights for the second and third panel. That means that the green and yellow and red lights will be operational.

Everyone's testimony is a part of this record. You don't have to read it all to us. Please don't.

The green and yellow and red lights means that you have five minutes to summarize your testimony. The yellow light will indicate that you are about to run out and the red light will mean that the gavel will fall and we will move on.

83-192 O - 94 - 2

Try to summarize when you see that yellow light turn on. As you would in a traffic intersection, try to complete your journey before the light turns red.

We are pleased to welcome Mr. Terence Coghlin, the Chairman, International Group of P&I Clubs; Mr. Richard Youell, Director of the Janson Green of Lloyd's of London; Mr. Hugh Bryant, Chairman of Shoreline Mutual Management and Mr. Stathes Kulukundis, Deputy Chairman of the Big Shipping Cooperative Committee on behalf of the Greek Shipping Cooperative Committee Norwegian Shipowners Association and Swedish Shipowners Association.

We will begin with Mr. Coghlin.

Let me admonish you. Summarize your testimony. We will light the green light as you commence, and try to cooperate with us as we do have an incredibly busy day.

STATEMENT OF TERENCE G. COGHLIN, CHAIRMAN, THE INTERNATIONAL GROUP OF P&I CLUBS; J. RICHARD L. YOUELL, DIRECTOR, JANSON GREEN LTD., ON BEHALF OF LLOYD'S OF LONDON; HUGH BRYANT, CHAIRMAN, MUTUAL MANAGEMENT LTD.; STATHES KULUKUNDIS, DEPUTY CHAIRMAN, GREEK SHIPPING COOPERATION COMMITTEE, ON BEHALF OF THE GREEK SHIPPING COOPERATION COMMITTEE, UNION OF GREEK SHIPOWNERS, NORWEGIAN SHIPOWNERS' ASSOCIATION, SWEDISH SHIPOWNERS' ASSOCIATION

STATEMENT OF TERENCE G. COGHLIN

Mr. COGHLIN. I hope Mr. Chairman, to beat all of your lights.

Mr. Chairman, I appreciate the opportunity to appear again before your subcommittee on this most important issue.

My name is Terence Coghlin, Chairman of the Managers of the United Kingdom P&I Club. I am here today as Chairman of the International Group of P&I Clubs, and as in November 1991, I am again accompanied by Lloyd Watkins on my extreme right, the executive officer of our Group, and by Robert Seward on my right, a partner in the managers of the Britannia P&I Club. And together we appear on behalf of all the Clubs in the International Group.

I have, Mr. Chairman, submitted a written statement for your record. All I want to do this morning, Mr. Chairman, is to invite you to stand back just for a moment and consider the important issues here in perspective.

There was no insurance crisis at the time OPA 90 was passed. The Exxon Valdez incident itself demonstrates this as the Club concerned paid the shipowner his $400 million cover without delay.

As you know, Mr. Chairman, the P&I Clubs provide their international shipowner members with a full range of cover against their liabilities worldwide. This includes oil pollution risk cover of $500 million per ship, per accident. That oil pollution cover has, as you know, responded to spills in the United States waters on a number of occasions in recent years. And despite what Mr. Sheehan said this morning, I think perhaps by accident, the Clubs continue to provide insurance cover. They object at this time only to additionally becoming guarantors.

The Clubs have lived up to their obligations and responsibilities under their contracts of insurance in every oil spill in the United States waters, as Mr. Sheehan was good enough to confirm to you a few minutes ago.

The truth is that our friends in the Coast Guard have in their rulemaking consistently underestimated the true value of P&I cover, not only to the shipowner members of the Clubs, but also to United States oil pollution claimants.

Consequently, there is an insurance crisis now—created, I am sorry to say, by the Coast Guard. This is because the Coast Guard, in its rulemaking, has focused exclusively on the need for an absolute insurance guarantee of the OPA 90 limits. The strange result of its inflexibility can best be illustrated, Mr. Chairman, by a very simple example.

Under its regulations, the Coast Guard would welcome into United States waters a 30,000-ton tanker which had insurance solely from a new and untried vehicle and limited to $36 million. For claims above this, the Federal fund—and thus, through that fund having to be supplemented, the U.S. taxpayer—would foot the bill.

At the same time, the Coast Guard would bar from entry into your waters, as lacking financial responsibility, a similar ship from an established P&I Club with a proven ability and willingness to pay claims up to $500 million. Moreover, the Coast Guard would do this at a time when many responsible shipowners are saying that $500 million is insufficient. Surely, sufficient flexibility could have been exercised to prevent this strange result, as you, Mr. Chairman, urged the Coast Guard so eloquently not only today but also at your November 1991 hearings.

Mr. TAUZIN. Mr. Coghlin, we are going to have to move on. During question and answer, if you wish to elaborate, you will have a chance to do that.

[The statement of Mr. Coghlin may be found at end of hearing.]

STATEMENT OF RICHARD L. YOUELL

Mr. TAUZIN. The next witness is, Mr. Richard Youell.

Mr. YOUELL. Mr. Chairman and gentleman, I appear before this subcommittee in November 1991, speaking as a Lloyd's underwriter, and I am grateful for the opportunity to appear before you again today. It is a matter of great regret that we all seem to be facing much the same difficulty now that we did two-and-a-half years ago.

Our written submission does not go into intense technical detail on the problems that we have identified with OPA, and most assuredly, I am not going to do so now. These problems have been rehearsed almost to exhaustion on our behalf with the Coast Guard and I know that many other interested parties have raised similar issues.

As insurers, our very existence is justified only by the writing of insurance policies and in the satisfaction of our obligations thereunder. Lloyd's is proud of a long history of working with worldwide clients to satisfy their insurance needs, be they ever so exotic.

We have long numbered shipowners and oil companies amongst those with whom we have worked most closely. For these reasons, if for no other, accept my assurance that it is no way our wish, nor

is it in our interest to fabricate difficulty or to invent complication in providing the necessary protection for those insured who are involved in the ownership of ships or carriage of oil by sea and the heavy liabilities incumbent on these commercially essential activities, nor do we wish to do anything other than to react constructively to the requirements flowing from any law that is passed by the Congress of the United States, be it in respect of pollution liability or any other matter.

We have spent two years debating the OPA issues and we have done it not out of caprice nor for our amusement, because we earnestly believe that there are fundamental and inescapable dangers for an insurer who becomes a guarantor under these undeniable Draconian rules. These are not exclusive to Lloyd's and must apply equally to any insurer who values the sovereignty and sanctity of its insurance contract before all parties.

An underwriter's responsibility isn't only with the providers capital that creates the security behind the policies that he issues—in the case of Lloyd's, these providers of capital are still overwhelmingly private individuals, not a few of whom are U.S. citizens. This make an underwriter's sense of duty all the more acute.

The responsibility also depends on all of those who purchase or have purchased policies of insurance, for if the funds of an insurer are exposed to a liability without limit for a special though small class of insured, then the integrity and security to which all other policyholders are entitled is put at risk. I address this issue at some length because it underlines our continuing inability to become guarantors under OPA.

Let us not quibble about the degree of uncertainty. Any threat to our solvency is too great a burden to assume. We have done all in our power to identify the public problems, to isolate the issue and to endeavor to resolve them. It is a matter of great regret to me that we have not been equal to the task of conveying our concerns to the Coast Guard or of achieving a consensus on the extent of the flaws in the OPA requirements.

In my judgment, and I can only speak as an individual underwriter and not on behalf of any other, the difficulties remain. We are more than ready to continue these efforts and would welcome any meaningful discussion in pursuit of a proper solution to the problem. But in the final analysis, it is a problem which the insurance industry cannot itself resolve nor should it be expected to do so.

Our priority remains only to make insurance promises on which we can deliver, and subject to that imperative, to continue to provide our clients with a broad and reliable protection for their liabilities.

It was London and Lloyd's in particular that first responded to the need for insurance for marine pollution. We developed the market to its present impressive size. Lloyd's bears the lion's share of the International Group's reinsurance programs as well as being a significant direct insurer and a provider of $200 million of excess capacity.

Very little of this insurance appeared sufficiently to be written into the U.S. market. Our wish is to continue this unique insurance, and it is frustrating that it is only the peculiar nature of the

administrative application of the financial responsibility rules that now stands in the way of our providing our insured with the protection they so desperately need.

Thank you.

Mr. TAUZIN. Thank you very much.

[The statement of Mr. Youell may be found at end of hearing.]

STATEMENT OF HUGH BRYANT

Mr. TAUZIN. Our next witness will be Mr. Hugh Bryant, Chairman of Shoreline Mutual Management Limited.

Mr. Bryant.

Mr. BRYANT. Mr. Chairman and Members of the subcommittee, thank you very much for giving us the opportunity to testify today. I am afraid I have to put you right, straight away, and say I am not Chairman of Shoreline, I am Shoreline's leading attorney and I am here to testify on behalf of the Shoreline management.

Mr. TAUZIN. Did we hear a rumor maybe that you were being elevated?

Mr. BRYANT. No.

Mr. TAUZIN. We stand corrected.

Mr. BRYANT. In fact, I am partner of the London law firm of Penningtons. We are one of five law firms which have come together to work for the Shoreline management company to create the Shoreline project.

My own personal experience does include a number of years as a manager of two P&I Clubs—one in a very junior capacity for the UK Club, and more recently, as chief underwriter and one of the directors of Liverpool and London P&I Management, Ltd. So I think I can claim to know a little bit about how P&I works.

My function today is to come to explain what Shoreline is, how it is organized, and what it will cost.

The genesis of the Shoreline project was quite simply the perception by a number of us that there was going to be a gap in the market for coverage for shipowners trading to the United States because the International Group P&I Clubs felt they were unable to become guarantors under OPA 90.

We felt that was a technical challenge to the insurance industry. It was not a question that the law should be changed or that really any kind of challenge of that kind was fruitful. We looked at it purely as technicians and said, OK, if that is what the law requires, how should the insurance industry respond to create the necessary coverage so that the guarantees can be given?

That perception was shared by a small group of appropriately experienced people; one former shipowner, two insurance brokers, a former P&I Club manager and several lawyers, and together they formed the original management company which gave the instructions to the law firms, which I have the honor of leading.

Shoreline is a P&I club. It is a mutual nonprofit organization. The terms of cover are set out in rules just like the International Group Club rules. And with your permission, Mr. Chairman, I am submitting a copy of the Shoreline rules for the record.

The only difference you will find between Shoreline's rules and the International Group Clubs' rules concerns the risks covered. Shoreline simply is confined to pollution from ships, and hazardous

and noxious substance pollution, and the other limitation is to the geographical area covered; it is limited to the United States.

And the other difference is the amount of cover provided which is $300 million for any one accident or occurrence as the maximum available from Shoreline. That limit was reached in consultation with the National Pollution Funds Center and it is designed to enable Shoreline to provide guarantees on behalf of the biggest ships likely to trade to the United States.

Shoreline has been designed to accept—to be capable of accepting into membership all types of ships, all categories of shipowners, in fact, every ship which currently has a certificate of financial responsibility backed by a guarantee from the International Group. So it has been created to fill the gap which the International Group had to leave.

Shoreline is buying reinsurance of $290 million in excess of $10 million, in a very widely placed program which is being placed by Willis Faber & Dumas, in London, and Willis Faber North America, Inc., in New York.

I would like to offer for the record a letter from Willis Faber to me of yesterday, which summarizes their efforts so far. It points out that since the rule came out, in the 20 days since the rule came out, they have targeted major geographical reinsurance areas including the U.S., London, Continental Europe, and Australia. And although this effort is at an early stage, "we have already received written and verbal indications of potential conventional and finite capacity in excess of $150 million." They go on to conclude that "it supports our confidence in supplying Shoreline with a viable reinsurance program."

They say that Willis Faber North America and Willis Faber & Dumas, Limited, the reinsurance arms of Willis Corroon Group, are prepared to devote substantial resources to provide Shoreline with the most effective reinsurance program. As you are aware, the Willis Corroon Group is one of the world's top five insurance groups and the second largest reinsurance firm, with 11,000 employees worldwide.

[The information may be found at end of hearing.]

Mr. BRYANT. So we believe that Shoreline will get its reinsurance contract with first-class security. It will provide, as I said, coverage up to $290 million in excess of $10 million, and an aggregate in any one year of slightly over $800 million.

The financial strength of Shoreline is the same as the financial strength of any other P&I club. Ultimately, it is the liability of the members to contribute supplementary calls.

It also means that if Shoreline ends up taking too much money because the risks in fact turn out to be not as great, it has the capacity to give the money back to the shipowners because it is a nonprofit organization. We have a tariff, which I would like with your permission to introduce for the record to demonstrate the proposed charges of Shoreline.

You will see that it distinguishes between tankers and nontankers. Nontankers will pay a small premium with comparison to tankers.

[The statement of Mr. Bryant may be found at end of hearing.]

Mr. TAUZIN. The time has expired.

We will move on and we will have questions later.

And finally we are pleased to welcome Mr. Stathes Kulukundis, Deputy Chairman of the Greek Shipping Cooperative Committee.

Mr. Kulukundis.

STATEMENT OF STATHES KULUKUNDIS

Mr. STATHES KULUKUNDIS. Thank you, Mr. Chairman. And good afternoon.

On behalf of the Greek Shipping Co-operation Committee, London, I am very grateful for the opportunity of testifying today. We and the Union of Greek Shipowners, Piraeus, represent the 120 million deadweight ton, Greek-owned, ocean-going merchant fleet registered under the Greek and other flags.

This fleet includes some 62 million deadweight tons of crude oil petroleum products and combination carriers. We are testifying today not only on behalf of ourselves but also on behalf of the Norwegian and Swedish Shipowners Association, with whom we have been cooperating over the three-year period since the COFR NPRM.

We have argued repeatedly over this period that the more fundamental issue to be addressed is not certification to OPA 90 and CERCLA limits, but, rather, the inadequacy of currently available pollution liability insurance in the face of virtual unlimited strict liability for oil pollution, arising under OPA and under the laws of several States.

With or without direct action, Mr. Chairman, we consider financial responsibility amounting to $1,500 per gross registered ton as required under the statutes to be extremely small in comparison to the actual liabilities faced and we, therefore, consider the struggle to achieve a direct action regime, based on these limits, to be largely irrelevant.

What would have happened under OPA if the Exxon Valdez had been owned by an independent owner without the deep pockets of a major oil company?

The vessel's pollution liability insurance, the $500 million P&I cover plus an optional extra $200 million available through the Clubs from the Lloyd's market, would have been exhausted. The reachable assets of the owner, a comparatively negligible amount in the vast majority of cases, would also have been consumed and the $1 billion Federal Oil Spill Liability Trust Fund would have been totally dissipated as well, leaving huge amounts unrecovered and unrecoverable.

In response to this colossal problem, our organizations have developed and proposed the mandatory excess insurance facility, or "MEIF". The complete proposal, together with pro forma financial statements and a draft legislative proposal, entirely independent of OPA, is included in our written submission.

This scheme would solve the COFR problem by providing the required direct action guarantees to OPA/CERCLA limits—the lower level on the chart—and would also provide excess insurance cover for U.S. oil pollution risks over and above the P&I cover to an aggregate amount of $2 billion, and this excess cover would be mandatory upon all ocean-going tank vessels engaged in the U.S. international trades.

The proposal calls for a federally chartered, budget-neutral, not-for-profit, independently run, government-sponsored enterprise, capitalized chiefly by bonds issued to the private investment community through the government agency securities market. Revenue would be generated by insurance premia, assessed on the assured vessels and charged on a per-voyage basis.

The MEIF would address the concerns of shipowners about inadequate pollution liability insurance and thus facilitate investment in modern, environmentally up-to-date replacement tonnage, and it would also protect the Federal fund which, we submit, is now at considerable risk and would remain so under any alternative proposal known to us.

In accommodating direct action, the scheme would not upset already existing arrangements for P&I cover and, furthermore, its capital structure would enable it to provide the high-level cover without conflicting with or displacing capacity for existing pollution cover.

These are important points, Mr. Chairman, because it has been argued that it may not be possible for the potential alternative solutions to the COFR issue to coexist with the P&I system. If that fear were justified, then we would be in danger of ending up with a regime providing less insurance cover at greater cost than what is available today, when what we need is more cover. That just doesn't make sense, Mr. Chairman; it would be a catastrophe for all concerned.

While we respect the Coast Guard's conclusion that the MEIF, although meriting further study, could not be adopted by them, we respectfully submit that it is by far the best proposal under consideration at this hearing. Not only would it solve the COFR issue without compromising the provisions of OPA in any way, but it would also ensure the availability of more funds to deal with serious oil spills. The scheme is fiscally sound, commercially feasible, fair and effective.

It is the only proposed solution that would take us forward rather than forcing us to struggle to stay put or to take a giant step backwards. It is the only proposal that could survive the next serious pollution incident. We, therefore, believe that the early enactment of appropriate legislation would clearly be in the interests of the people of the United States.

Mr. Chairman, the time for the MEIF is now and its proponents, the shipowners' associations of Greece, Norway and Sweden urge the United States Congress as a matter of priority, to enact legislation providing for this important measure. We would be pleased to work with this subcommittee or with any committee or agency of any branch of the United States Government in any appropriate fashion aimed at bringing this about.

Thank you very much.

[The statement of Mr. Stathes Kulukundis may be found at end of hearing.]

Mr. TAUZIN. Thank you gentlemen, we will now go to questions by me and Mr. Gilchrest.

Mr. Bryant, I have a copy of the letter that you referred to from the broker. And I also have that letter of solicitation. And I want to quote from the letter of solicitation.

The letter of solicitation says that: We, therefore, now seek only your nonbinding confirmation of your interest in supporting the program, so that it can be carried to the next step after the oversight hearing. In this connection, we have attached a sample letter to be used as a guide. We wish to stress this confirmation of your interest is not binding, but will enable the managers of Shoreline to demonstrate the viability of this concept to government officials.

It sounds like a publicity campaign. Is that all it is; or is Shoreline really going to get reinsurers to line up, as your testimony indicates, which is absolutely essential to the financial viability of the structure you propose?

Mr. BRYANT. Mr. Chairman, you have the advantage of me in the sense that, you know, when I have a dog, I tend not to bark myself. And therefore, I am not actually privy to the letters which our brokers have actually been writing to their chosen market.

Mr. TAUZIN. Have you not seen this letter?

Mr. BRYANT. What I do think is that when the brokers report to us that they have received interest from those markets, and the letter, of course, was written in order to be demonstrated to you, a company of the size and standing of Willis Faber doesn't actually make statements such as it has made without some confidence that it is going to be able to do the job. I don't know what letters they have actually received from their various——

Mr. TAUZIN. Is that a problem—I will give you a copy of this letter, if you like.

Mr. BRYANT. With great respect for the Chairman, of course, I have seen that letter. The thing that I will assure you, though, is that there are five well-founded law firms who are all charging quite healthy sums, who are basically depending on the client, the Shoreline Management to keep us fed and watered until the rule is in effect and the Shoreline project can start underwriting. That will require a level of commitment to the various investors behind Shoreline of several million dollars. If we didn't believe as professionals that this whole project was feasible, we would not be here today.

Mr. TAUZIN. But the reason I raise it is, obviously, if your brokers are only requesting nonbinding confirmations of interest and stressing the nonbinding character of those letters, I want to know what kind of letters have they received from people to which they have referred in the letter that you quoted to us?

Mr. BRYANT. Yes, Mr. Chairman, I think what was in the minds of the brokers and what we were perhaps hoping to do was to actually have some letters to show to you at this hearing. I have to say that in the letter which we have asked for you to accept in the record from Willis Faber, you will see on the second page that they have, in fact, experienced—some of the reinsurers contacted have, in fact, experienced some pressure on them from other people.

Mr. TAUZIN. They claim to, anyhow.

Mr. BRYANT. They claim to and they are a little reluctant until the contract is signed and sealed to let their names be known.

Mr. TAUZIN. They defined the letters they received as both written and verbal indications of potential conventional and finite capacity in excess of 150 million; what do they mean?

Mr. BRYANT. Perhaps I can help you out in this way. What we are trying to do is create one of the biggest reinsurance contracts in the world. The biggest is the International Group of P&I Clubs' reinsurance contract. The Shoreline one will not be as big, but it will certainly be one of the very big ones.

The International Group's reinsurance contract has been placed for many, many years now and it still takes the leading firm of Lloyd's brokers who formed that, several months to put the details into place each year. In Shoreline, we are having to do a similar job and we had to start on July the 1st, because until the requirements of the rule were known, it was not possible to go to any reinsurers with anything more than an in principle inquiry.

The project for the reinsurance placement started 20 days ago. I think to have got to the stage where Willis Faber is prepared to say that we are assured of getting the 150 million of the 290 required in 20 days——

Mr. TAUZIN. They have not said that. That is my point. All they have said is that they have received written and verbal indications of potential capacity. And when I read their letter of solicitation, they have gone to great lengths to tell these people; when you get back to us, make sure that you know and we know that nothing is binding.

Mr. BRYANT. I think that it is a little bit sterile here to say to you what I think is in the mind of the reinsurers or whatever. What I would point out to you is that Willis Corroon's people have said that they feel confident that this program can be placed and that letter says that loud and clear. And we believe them.

Mr. TAUZIN. All right. I want to ask you—and, Mr. Coghlin, if you could also join in this discussion—to play against one another a bit here.

You mention in your testimony, Mr. Bryant, that as such, Shoreline's friend, like any other P&I Club, will be the function and the strength of its shipowner members.

The letter from your brokers indicates that one of the unknowns is: How are the P&I Clubs going to use the existing reinsurance program, thus, even more capacity might be available to you if P&Is are available to you as insurers. I read.

What is the difference between Shoreline and a P&I Club, if you end up relying upon reinsurers to make up the 300 million liability cover that you propose to offer to shippers?

Mr. BRYANT. The International Group, as I am sure Mr. Coghlin will tell you, has a comprehensive reinsurance program. I think it is the biggest in the world. Shoreline also is planning to have a reinsurance program. That a P&I club has a reinsurance program doesn't make it any less than a P&I club.

Mr. TAUZIN. Exactly as P&I Clubs now operate, as you pointed out, Shoreline proposes to operate on the basis of its shipowner's strength. That is the foundation of P&I Club strength. You say that is going to be the foundation of Shoreline's strength.

Both you currently operate with reinsurers behind you. They operate with reinsurers and you propose to operate in the same way. What is the difference between Shoreline and a P&I Club in the end?

Mr. BRYANT. Shoreline has in its Rules a specific rule which permits it to issue COFR guarantees.

Mr. TAUZIN. So the difference is you would subject yourself to these rules and the P&I Clubs would not, but that is the only difference.

Mr. BRYANT. That and the differences in our levels of liability exposure.

Mr. COGHLIN. I think your exchange with Mr. Bryant is very fair. It is a one-risk, one-area club but structured as our individual clubs are, and with a 300 rather than a 500 million dollar limitation on oil pollution liability cover.

And in terms of playing against Mr. Bryant, which you kindly invite me to consider doing, I have no interest in doing that at all. I wish him well.

Mr. BRYANT. I am grateful to you.

Mr. TAUZIN. And next to you both, Mr. Kulukundis is offering a new concept of a government-sponsored program of bonded insurance. Why government-sponsored? Why can't the markets fund a bonded insurance program for the shippers?

Mr. STATHES KULUKUNDIS. Because, Mr. Chairman, our inquiries with the commercial insurance markets indicate that that capacity is not there at the moment. And we can—we feel that the government-sponsored nature would be required to get the scheme off the ground until it were up and running, with respect, it would be self——

Mr. TAUZIN. Help me on this. I thought we created a government-funded insurance program for oil spills when we created a billion dollar government fund, and that we would supplement it under OPA 90 with individual evidence of financial responsibility in order to make sure that the players who operate are going to be responsible for what they do. As I understand good insurance principles, it is also supposed to make the players more careful about the way they operate and how they are prepared to respond to a spill as they have residual liability under the system; am I wrong? Haven't we created a government-sponsored insurance fund under OPA 90 to the tune of a billion dollars.

Mr. STATHES KULUKUNDIS. The Federal fund, Mr. Chairman, does protect potential claimants against the possibility of the owner not being able to meet the liability.

Mr. TAUZIN. Isn't that insurance?

Mr. STATHES KULUKUNDIS. That is protection available to the claimant. It doesn't provide protection to the shipowner who is most concerned at the possibility of——

Mr. TAUZIN. But at the bottom of all of this is insurance for the claimants. And the reason we passed OPA 90 was to insure the claimants, citizens of this country were protected against oil spills. And that somebody paid the bills. So we told all the players, chip in some money in advance to a Federal fund, which is going to be an insurance fund, in case any one of you are incapable of meeting the needs of a claimants in America who suffer an oil spill. Again, unless I am all wrong, I thought we had established such a fund.

We have a vote on, and my time is extremely limited and so we will recess then while I run to vote.

[Recess.]

Mr. TAUZIN. The committee will please come to order.

My apologies. When we hit the Floor we found out there were more votes. We were in the midst of some questions to the second panel. I wanted to renew some of those in a minute.

This is to all of you in general. My understanding is that for ships to qualify by December, they are going to have to make some decisions as early as October in terms of leaving the Gulf with supplies. I want to talk about the timetable just a little bit.

Mr. Bryant, we talked a little bit about what is going on in terms of your company trying to put together its reinsurance. We talked with the Coast Guard a little bit about when they think they are going to be ready to either certify you or other insurers, and they gave us some indication, at least, of what they might do if things don't work out. But here is the question.

If, in fact, shippers are going to have to launch or not launch in October vessels destined for ports in the United States, and they have to qualify by December, is it not true that before they launch those vessels, they are going to have to give assurance that they meet the COFR requirements and be certified to enter U.S. waters or the launch itself may never occur?

Anyone want to handle that?

Mr. BRYANT. I can talk about what I call the critical path, which in setting up a new P&I we are going to have to follow. And we can relate that to a target time so you can then assess how your hypothetical shipowner leaving the Gulf is going to fit in with that.

Mr. TAUZIN. Let's do that. Let's assume that you are plotting ahead. You are going to file for acceptance with the Coast Guard, that you have got a timetable in which your brokers are going to get in reinsurance for you. When do you expect to file with the Coast Guard with adequate reinsurance to satisfy the Coast Guard of our financial capability to be certified as a properly, financially capable insurer and guarantor?

Mr. BRYANT. We anticipate that to get to that stage, Shoreline needs to do a number of things. First of all, it needs to be incorporated. It is incorporated.

Second, it needs to get its reinsurance program fixed.

Third, it needs to get its leading shipowners to join its board so that they can control its final shape. Then it needs to launch its bond offering so that it actually has capital money available in case there is a major claim on day one. And when it has got all of that, then it goes to the Bermudian authorities to get its formal permission to underwrite in Bermuda and it goes to the Coast Guard at the same time to get its permission to act as a guarantor. Now, we anticipate that that whole process should be complete during the month of October.

Mr. TAUZIN. During the month of October. And obviously then you are going to take applications after you have been authorized to act pursuant to Coast Guard permission. How long will it take you to examine applications for coverage.

Mr. BRYANT. Because it is going to be a large job, the Shoreline requirement has been to set up a program which could accommodate all the ships which are currently covered by COFR guarantees issued by the International Group of P&I Clubs. Now, the Coast Guard tells us that that is somewhere slightly over 15,000 ships.

For that reason, Shoreline is underwriting on the basis of a tariff so that it is a very mechanical business to work out what each ship would pay and what its requirements would be.

We have taken the precaution of setting up data bases so that in fact all of those ships are now on data bases. The majority of the main shipowners are already in touch with Shoreline. So an awful lot of the preparatory work has already been done.

Mr. TAUZIN. Granted, you have named a number of things that have to fall into place. Corporating should not be difficult since you have a lot of lawyers on board, but you do have a problem of getting all of your reinsurance together, you do have a problem of getting shipowner acceptance and participation on your board. As you pointed out, the success of your venture depends upon the strength of the shippers themselves.

You have to make your bond offerings. You have to at some point, not only go through the process of going through the Coast Guard for permission to operate, but you have to also come up with a schedule of tariffs or premiums by which shippers are going to go in to apply for and buy this coverage.

Mr. BRYANT. Mr. Chairman, they exist already. The draft tariffs are in the docket which is being submitted to you.

Mr. TAUZIN. Right. But you will have to eventually do more than draft them. You will have to tie them down and offer them to shippers.

Mr. BRYANT. The difference is that when the reinsurance contract is fixed, the reinsurers have to indicate that the tariffs are acceptable to them. Every indication that we have had is that the tariffs are acceptable.

Mr. TAUZIN. You did not anticipate all of these things would fall in line. Obviously, you would not be here so I would not presume that you would give me an answer other than you expect it all to hatch, but what happens if any one of these do not fall in place and you are not able to offer this by October? My understanding is that shippers are going to have to be insured by October to launch some of these shipments to America.

Mr. BRYANT. No. I think with respect, Mr. Chairman, that is not correct.

Mr. TAUZIN. Why is that wrong?

Mr. BRYANT. The rule requires self-propelled tankers to have evidence of financial responsibility which doesn't actually mean COFRs. It means the new guarantees on December the 28th. They don't need to have them in October.

Mr. TAUZIN. We are told and what I hear from shippers is that if we will be required to have a COFR by December 28th then we are not going do launch in October without having one then. That is the conundrum that I think some of shippers find themselves in.

Mr. BRYANT. I very much doubt, Mr. Chairman, that many shipowners would pay premiums for an insurance for which they don't actually need and they don't need this insurance before December 28th. So I think you will find that everything has to come together on December the 28th and not before.

Mr. TAUZIN. But the point they are making, Mr. Bryant, and please address it if you can, is that if they do not have the confidence that it is available to them when they have to launch, then

it makes it very difficult for them to make the decision to launch a journey to the United States loaded with oil.

Mr. BRYANT. I am very sympathetic to that and we have spent a lot of time and effort actually meeting shipowners worldwide and actually discussing with them exactly how the whole system is being set up precisely with the purpose in mind of building their confidence. Present in the morning session was a director of the investment bank that is actually going to underwrite the bond, for example. You know that the law of the United States precludes people from identifying bond underwriters before the underwriting is actually done because of the "jumping the gun" provisions, but they were here.

The leading shipowners who are going to go on to the board, we know who they are. A lot of the work is all there. The understandings are all there. This is not something which is just an airy-fairy program.

Mr. TAUZIN. Well, we are going to hear from some shippers in a later panel about this. I would invite everyone's attention to these concerns and would appreciate submissions to the committee of information regarding these timetables so we can interact with the Coast Guard in these rules on this matter. Of course, I invite any of your comments to the committee.

Let's go back to where we were before we recessed. We have these new insurance lines that are proposing to be a new form of P&I, and reinsurance is critical to their success. Mr. Youell, the current system of insurance involves a P&I Club for the most part, perhaps some other participating coverage, and then an umbrella or reinsurance coverage by Lloyds of London or others; is that correct?

Mr. YOUELL. I would describe it more that the P&I Clubs take the whole risk and we, as reinsurers, offer reinsurance at a level to them.

Mr. TAUZIN. Right. If that is the current status of things, what would be the function of Lloyd's of London in a new arrangement like the new form of insurance to be developed that Mr. Bryant represents. P&I Clubs may or may not come in as reinsurers of that new form of insurance. What is the role of Lloyd's of London at that point? Would you be a reinsurer to the reinsurer?

Mr. YOUELL. Lloyd's of London is only one of the possible reinsurers that might express an interest in reinsurance capacity to any new——

Mr. TAUZIN. Directly to the insurance?

Mr. YOUELL. No. As a reinsurance of one of these new ventures. I can't speak for whether anybody in Lloyd's would express an interest in it or has already done so.

Mr. TAUZIN. You have indicated in your testimony today that under these rules, you don't feel like you would want to participate as a reinsurer as you have been with the P&I Clubs. What would make you want to participate with these new companies any more than you would participate with P&I Clubs if they subjected themselves to these rules?

Mr. YOUELL. Lloyd's operates in two ways here. One is a direct insurer, and as a direct insurer where we write, particularly the 200 million in excess of 500 million, we are their direct insurers

and we have examined the question of becoming a guarantor and found that it is something we will not do.

Mr. TAUZIN. So your testimony is that you would not serve as a guarantor under these rules. Is your testimony also that you would not serve as a reinsurer to any of the guarantors?

Mr. YOUELL. As a direct insurer, one would not wish to do it. One would naturally look with some care when operating as a reinsurer of somebody who has agreed to become a guarantor.

Now the situation as a reinsurer, you are somewhat isolated. You are one step back. But at the same time, quite clearly, if you are reinsuring somebody who has agreed to become a guarantor, the likelihood of the frequency and size of loss would increase. And at that point, one of the considerations is how much money does it cost to offer that reinsurance? And two, how secure as a reinsurer do you feel that you will actually be insulated from the problems of becoming a guarantor even though you are one step behind?

Mr. TAUZIN. Mr. Coghlin, can you see any improvement in the security of insurance under these rules than currently exist with P&I coverage?

Mr. COGHLIN. I think, Mr. Chairman, I possibly ought to, with your permission, just pick up a point which you made in questioning Mr. Youell. If I may, with your permission, do that.

Mr. TAUZIN. Certainly.

Mr. COGHLIN. You put to him a situation in which the existing P&I Clubs might become the reinsurers of one of these new vehicles.

Mr. TAUZIN. Yes.

Mr. COGHLIN. And asked Mr. Youell whether he would like to reinsure us in that situation.

The possibility of our being brought in to reinsure one of these new vehicles I think is very low.

I am not aware that that forms any part of their thinking. And were it to do so, I think it is very unlikely that the International Group clubs would wish to become the reinsurers of one of the new vehicles. As Mr. Youell said, having decided that we are not going to do this thing and become guarantors, for us to be invited to reinsure somebody who is going to be offer themselves in that way would be rather surprising.

Mr. TAUZIN. Well, then, Mr. Bryant, what does Willis Faber of North America Inc. say when one of the uncertainties that needs to be cleared up is are how the P&I Clubs going to use their existing reinsurance program which could make even more capacity available to us. Could you explain that?

Mr. BRYANT. I can clarify that fairly easily.

What Willis Faber was referring to there was the fact of a discussion which has circulated around and really is very much a tentative rumor. We have not had any direct discussions with anybody, but Willis Faber had heard in the marketplace a rumor that the International Group were perhaps considering pulling out of North American oil pollution coverage altogether so that they would not provide the $500 million at all for oil pollution coverage in the United States. Therefore, the gap which had to be filled, if at all, by Shoreline, would have increased from $300 million to $500 million. And, obviously, if that coverage was not being offered

by the International Group, the reinsurers on the International Group's reinsurance would be available to reinsure somebody else because they wouldn't be doing the job for the International Group.

Mr. TAUZIN. Are we hearing from them they may not be too interested in doing that?

Mr. BRYANT. Well, I think, just taking the points in order, the point therefore is that what Willis Faber was talking about was a highly theoretical situation. Nobody has any evidence that the International Group is planning to change the nature of its coverage. And I think that, really, you should look at it simply on that basis. As to what the likely attitude of reinsurers is, we believe what Willis Faber told us about a particular group of reinsurers. Mr. Youell has obviously testified to the attitude of his group of reinsurers in Lloyd's.

Mr. COGHLIN. Mr. Chairman, as the rumor has been mentioned—quite rightly by Mr. Bryant in explaining this comment of Willis'—I should reaffirm to you what I told you in 1991 and what I am telling you in the testimony that I filed with you today, and that is to say that the International Group hopes to be able to continue to provide the cover.

In other words, there is nothing in this rumor. We are striving to continue to provide the cover as we do today, and as we have done continuously in the past. Our hope would be that we are able to continue to provide that cover and that would be our wish.

The only threat to that is, as we have said in our written testimony, if in due course it falls out that the natural resource damage assessment rules become—if I may put it this way—the last straw which breaks the camel's back, then we might have to consider putting to the shipowner Directors of the clubs whether they still can see their way to providing the cover. But that is a separate issue from today's hearing. And I reassert that we are providing the cover. We wish to go on providing the cover. And any rumor to the contrary is unfounded.

Mr. TAUZIN. We certainly would not pass that rumor on to anyone else.

Mr. COGHLIN. It is just to keep your record straight, Mr. Chairman.

Mr. TAUZIN. Mr. Kulukundis, let me go back to the question we left when we recessed. The question was if the private marketplace will not provide such a $2 billion bonded system of indebtedness for coverage under the COFRs, why it is that our government in America would want to do that when we have already installed a $1 billion insurance fund for the claimants here in America who can make claims against responsible parties in an oil spill. The question is why do we have to do it twice?

Why do we need another fund when we have set one up already?

Mr. KULUKUNDIS. Well, the Federal fund, Mr. Chairman, is not an insurance—it is not insurance. It is a trust fund which protects the claimants. The legislation provides for the fund to subrogate, to claim any amounts that it pays out from the offending shipowner.

Mr. TAUZIN. But you understand those of us who have not grown up in insurance law and intricacies of insurance contracts—I am one of them I must confess—find it difficult to understand the dif-

ference between a trust fund that pays claimants and then has subrogation rights against responsible parties that quacks like an insurance fund. If it isn't an insurance fund, it sure looks like one. I also keep hearing from the government officials who run the fund that they don't want it to be an insurance fund. They never want to use it except to cover a deficit in this country, but it sure sounded like an insurance fund when we created it.

Mr. KULUKUNDIS. Well, the liability, Mr. Chairman, to the shipowner remains over and above the available insurance. The insurance that the shipowner has. The——

Mr. TAUZIN. Isn't that true with insurance, if I have an automobile and I insure it and my insurance does not cover all the damages, I am liable for the balance.

Mr. KULUKUNDIS. Precisely.

Mr. TAUZIN. The only difference here is that in this case I am also liable in subrogation for the full amount of the insurance coverage back to the fund; right?

Mr. KULUKUNDIS. Indeed. We have available insurance at the moment from the P&I Club of 500 million. We have the 200 million in excess of 500 million available through the Clubs from the Lloyd's market. And in excess of that figure, the shipowners are exposed. But—and that quite clearly worries many of our members.

But in addition to that concern on the part of the shipowners, we submit that the fund, the Federal fund which kicks in at above these levels and will then be forced to take recourse against the shipowner and will find that the assets of the shipowner are simply not sufficient to meet these claims, we are talking of vast sums, 3.6 billion paid thus far in the case of the Exxon Valdez, and many, many billions more in punitive and compensatory damages still pending. Now in that scenario, in the scenario of an Exxon Valdez-type incident, the insurance—the available insurance, the 700 or the 500 million is used up, as I said in my statement. The assets of the shipowner vanish, and the fund is completely dissipated, as well. And it is that situation that we wish to address with the MEIF. The MEIF gives protection not only to the shipowner, but also to the Federal fund.

Mr. TAUZIN. Well, I am simply left with the following impressions, and I will yield to my colleague. The impressions I have is that this interim final rule is literally pushing out of participation the current forms that have been reliable and have been out there, and is inviting the formation of new forms that look remarkably like the old forms, but may not have the availability of some of the reinsurance the old forms had.

And we are being asked to remedy it with another government-sponsored insurance program if this one doesn't work. We are also left with the very risky business of hoping that if these new insurance forms work at all, they will be in place in time for shippers in October to rely upon them. I have grave concern that there are a number of things that can go wrong that might not allow that timetable to be fulfilled. Then, we are left with a Coast Guard response of, well, if all that happens, we may suspend these regulations or go through some sort of selective enforcement.

Again, I must tell you, I am not comfortable with what I am hearing today. I believe if more Members of Congress were hearing

this, there would be a lot of discomfort in these halls. I suspect as the message gets out, that level of discomfort is going to spread.

My friend, the Ranking Member, Mr. Coble is here, do you have additional questions, Mr. Coble?

Let me yield to Mr. Laughlin, any questions?

Mr. LAUGHLIN. I do for—and I apologize for not being here earlier but, Mr. Coghlin—am I saying that right? Coghlin? My name is spelled very similarly but those of us with Scotch-Irish names have them pronounced one way and spelled a different way.

Mr. COGHLIN. It should be Coghlin, but to help the native English amongst whom I live, we have Anglicized it to Coghlin.

Mr. LAUGHLIN. I am thankful to my ancestors for dropping the "Mc". Down south we pronounce it the proper way: Laughlin.

Mr. TAUZIN. Mr. Laughlin, we are——

Mr. LAUGHLIN. I didn't want to offend the gentleman before I asked him a question.

Mr. TAUZIN. We are still two great nations separated by a common language. You know that.

Mr. LAUGHLIN. I am interested in the certification and the P&I position on pollution insurance. I come from a part of the country where we have numerous pipelines.

We have not enough highways, but the ones we have manage to cross rivers and bayous and bays and estuaries, and early on it was one of my constituents was running barges out to the Gulf of Mexico platforms that were complaining that they couldn't get insurance. And next I was hearing from the shrimpers in my district that they couldn't get coverage. And then, lo and behold, of all the people that shocked me were the 18-wheel tank trucks which I could not envision traversing the navigable waters of our country, but they have been told that they can't get pollution insurance because they may be in a vehicular accident or sustain a leak over one of the bridges over navigable waters for which they can now get no P&I Club oil spill pollution insurance coverage.

And I would like for you to address—and I am certainly sorry more members of this committee—and I can't fault them much, because I have not been here myself, so I know that they are busy on important things, but many on this committee opposed placing limits of liability.

Could you give us a short insurance lesson on why the P&I Clubs which you represent will not write this insurance because there is no limits? And if there is a limit definition or some high exorbitant range that even if we had that, if your group would be willing to write oil spill pollution insurance, if that is possible? Could you do that for this record?

Mr. COGHLIN. I think, sir, we may be being drawn in here from the ocean, which is where essentially we write risks, into an inland environment, which would not be our natural place. And I just fear I may be the wrong person to field your question. It may be that Mr. Youell could help more. Generally our business is blue water, ocean-going ships and I fear anything I may say would be ignorant.

Mr. LAUGHLIN. I appreciate that, did you understand my question?

Mr. YOUELL. I think so, sir. Am I right is one of your concerns having to do with pipelines crossing rivers?

Mr. LAUGHLIN. Yes, really underwater, both ways.

Mr. YOUELL. I can only answer as an individual underwriter. Lloyd's does provide some coverage, a very limited basis for those sorts of exposures. But again, any question of certification or becoming a guarantor for such risks would prove very unattractive.

As far as the inland waterways are concerned, as was mentioned this morning, I think most of the insurance there is written by a water quality improvement syndicate. And as I understand it, they are more content with the requirements than are we as direct insurers of ocean tonnage.

Mr. LAUGHLIN. I yield the time.

Mr. TAUZIN. The chair will recognize Mr. Gilchrest for questions.

Mr. GILCHREST. Thank you, Mr. Chairman. I take it there is no one on the table giving testimony from the Bronx or Brooklyn or Los Angeles? I like the accent, though.

I just have a couple of quick questions and then I want to yield to the Ranking Member. And Mr.—and I will pronounce it wrong—Mr. Coghlin, was that correct?

Mr. COGHLIN. That is fine. Thank you.

Mr. GILCHREST. Do you currently pay larger premiums for vessels which travel to the U.S. as opposed to those who travel to other places around the world?

Mr. COGHLIN. Yes, we do and specifically in the area of tankers bringing dirty oil into the United States. There is a schedule of surcharges for the fact that they are trading into United States waters where the cost of cleanup of any spill which may occur is simply much higher than is generally the case in the rest of the world.

Mr. GILCHREST. What do you mean by "dirty oil"?

Mr. COGHLIN. I would not include in that products and so on, but I am talking about crude oil imports.

Mr. GILCHREST. Would you say they are higher here or would the reinsurance premiums—did they go up as result of the Oil Pollution Act of 1990?

Mr. COGHLIN. I think to be fair, it is a combination, sir; introduction of the OPA 90 and of the general trend in the cost of oil cleanup in this country and of attendant damages.

Mr. GILCHREST. Could the market have already factored in OPA 90 into the reinsurance premium costs?

Mr. COGHLIN. They have done so and we, of course, are paying those additional reinsurance premiums—which is why we think it is fair to pass some of those extra amounts on to the shipowners we insure, to make sure that we are not unfairly treating those who are not participating in the additional risk of oil pollution in the United States from tankers.

Mr. GILCHREST. The Coast Guard interim rule strongly maintains that OPA 90 does not subject insurers and other providers of financial responsibility to unlimited liability. Could you explain why P&I Clubs disagree with the Coast Guard's assessment?

Mr. COGHLIN. Yes, we are grateful to the Coast Guard for the attempt that they have made to add, I think, a moat and barbed wire, to quote their written testimony this morning, around the castle which is said to have been created by OPA itself in terms of protecting the guarantor from unlimited liability. Our worry remains, despite the best efforts that the Coast Guard have made,

and we accept that they are the best efforts that the Coast Guard could make. We are very concerned as insurers with substantial reserves and a substantial ability to make calls, further supplementary calls, upon our members (which is a well-known feature of our system).

In the event that there is a very large spill, a shipowner is most certainly going to lose his limit under OPA 90. I agree with the comment made this morning from the environmentalists to that effect. We are not expecting in a big spill that the shipowner will hold his limit. We will then, if we had accepted guarantor status, we would then be staked out, in effect, before an American court, either Federal or State or maybe both, with our massed assets available. And our only defense against being plundered as a very obvious deep pocket in that situation would be the defenses which had been written into OPA and now into the Coast Guard certificates. They should be enough.

We believe, however, there is still a significant risk that, faced with the huge claim that I am contemplating, with uncompensated victims before the court and with the knowledge that we are a seriously deep pocket, it will be more than judicial flesh and blood can bear to send away those uncompensated claimants empty handed and to allow us to withdraw with our deep pocket still full of our reserves and our ability to make calls on our members.

How exactly the defenses that the Coast Guard have described will be circumvented I can't tell you because I am not sufficiently ingenious. All I know is that when the day comes we will be quaking in our boots in that situation. And the bet we are making is a huge one. Our whole worldwide system will be on the line at that point with a single claim in this country. And we, I am afraid, do not have sufficient confidence in those defenses—despite the fact that we cannot tell you exactly how they will be breached—to quiet our continuing concern about being exposed to unlimited claims in that situation.

Mr. GILCHREST. So you feel that the Coast Guard is not sufficient to defend you from what you just described as this beast carrying the wire cutters to cut the wire around the castle?

Mr. COGHLIN. You put it much better than I, sir.

Mr. GILCHREST. A two-part quick question. What percentage of your business is U.S. waters? If you stopped insuring vessels coming to the United States, and if you did—and I hope you don't—but if you were to pull out, so to speak, and stop insuring vessels coming to the United States, what impact would that have on P&I Clubs if it is significant, what would you do?

Mr. COGHLIN. Firstly, let me echo your comment, sir, that we very much hope that we will be able to continue to give that cover. The proportion of our ships trading to the United States is quite high, both tanker and dry cargo. Because of the magnitude of your economy a lot of ocean-going ships come here and our proportion of the total of those ships coming will be very high. We are probably insuring somewhere between 90 and 95 percent of those ships which are coming to and going from your shores. As a proportion of the world fleet, I would be guessing if I produced a figure, but it must be quite a high percentage of the total ships of the world

who trade to the United States. Most of those will be covered by us.

Were we to be driven away from this risk, which is indeed the threat that is being built up here, we still have plenty of risks to insure in the rest of the world, both for those ships that come here and also for those ships that never come to the United States waters. But certainly our business would be quite significantly reduced.

What would we do? I think we would slightly curtail our reinsurance program and we would continue as before.

Mr. GILCHREST. Thank you, I will yield to the Ranking Member.

Mr. COBLE. Thank you, Mr. Gilchrest, and I will be very brief.

To my friend from Great Britain, I am going to address you as Mr. C, that way you will not make any mistake. Gentlemen of the panel and Mr. Chairman, I apologize to you all for my having been here, there and yonder. Oftentimes here we must be in five places simultaneously and today has been one of those days.

Mr. C, Mr. Coghlin, I should have stuck with Mr. C, you touched on this, I think, with Mr. Laughlin's question. I think you touched on it as well in responding to the question put to you by the gentleman from Maryland. But permit me, if you will, to be a little more specific. And I am now addressing the fears that obviously are present, and perhaps for good cause, in the P&I community.

Lay out for me, if you will, a specific chain of events which would illustrate how becoming guarantors could destroy the worldwide P&I insurance structure. And I don't mean this question to be adversarial. I am asking, I am not quizzing.

Mr. COGHLIN. When we look, Mr. Coble, at the sort of damages which we see flowing in against Exxon, even under a pre-OPA 90 claim, we can see that we may be talking billions of dollars here. Were we unable to hold our limit in the face of one of these claims as guarantor, then we should certainly have to pay and we could be talking about many millions of dollars.

That is going to have two very serious effects. The first is that we will be sending a very unpleasant message to our reinsuring underwriters. We shall be cleaning out, a total loss on that policy for the year. We shall be claiming to the maximum extent of our reinsurance, which will obviously cause them great concern, and hurt us when it comes to renewing that policy at the end of the year.

Secondly, we shall be having to make substantial supplementary calls on our own members if our own reserves at that time are not sufficient to deal with the sort of claims we are talking about.

Moreover, there is no rule of nature which says that these big claims will come neatly one in one policy year and one in the next. If you can have one Exxon Valdez—and we don't need really to talk about a claim quite that big—in a year, then you can have three, four or five. The effect on our ability at that stage to get reinsurance is going to be devastating. I am not now talking about price. I am talking about capacity.

Mr. COBLE. You are not talking about price, you are talking about what? Oh, capacity. I didn't hear the word.

Mr. COGHLIN. Our ability to continue to bind reinsurers into our contract, regardless of price. Gradually at that point our system is, I think, beginning to unwind.

And that seems to the shipowners who are the directors of the clubs—not people like me, but shipowners themselves—may lead them to say, well, this whole situation is impossible to bear here and that is why we are not willing to become guarantors. However, we are still willing to be the indemnity underwriters of the shipowners as we are at present. Mr. Seward would like to add, if he may.

Mr. COBLE. I thank you for your response. That is a very clear-cut answer.

Mr. SEWARD. If I could add.

Mr. TAUZIN. Would you identify your name for the record?

Mr. SEWARD. I hope it is more pronounceable. It is Seward. And I believe that one of my ancestors bought a chunk of Alaska for you. And he pronounced it the same way.

Mr. TAUZIN. Correctly identified as the folly, I believe.

Mr. SEWARD. One of the other major problems with becoming a guarantor is that it turns an insurer such as ourselves, an indemnity insurer for shipowners, into, in effect, the insurer of the American public, which is a very different position to be in. And it exposes us immediately to direct action as if we were insuring the claimants.

Mr. Youell has much greater experience at the sort of problems which can be faced by insurers in the United States, but I think it is not unreasonable to describe them as horrific, your judges and your jurors don't look kindly on insurers and still less kindly on foreign insurers. At the moment we are protected from those horrors because we don't on the whole insure the American public.

We insure mostly foreign shipowners and there are well-established means for dealing with disputes under the cover, which are in fact extremely rare. If we were to become guarantors in the United States, we would be sued in a United States court in front of a United States jury in what is bound to be a highly emotional situation such as would arise after a large spill.

And I think it is not unfair to say that we would then be nervous of the sort of treatment we would get in such a forum. In addition there is the exposure to punitive damages, bad faith actions and all that type of stuff, which would be a brand-new and completely different exposure directly on us as guarantor and nothing whatsoever to do with the incident itself and the pollution arising from it and that is a very major consideration. I would be happy to try to amplify that. It is a second exposure and very frightening.

Mr. COBLE. Thank you. I thank you for the illuminating answers gentlemen. And I thank the gentleman from Maryland for having yielded to me.

Mr. TAUZIN. I thank both gentlemen.

Mr. Laughlin, do you care for additional comments?

Mr. LAUGHLIN. I apologize to the gentlemen again. I tried to drag you too far inland, so I will not do that in my next question.

I would like any of you to respond to your written concerns in your statements that you will be without policy defenses as one of your objections why the P&I Clubs won't provide coverage. And ex-

plain why this is a problem. I think I understand a little bit about failure to pay the policy being a defense. Could you give us the reasons why you are concerned. And it sounds like you are saying that any policy defense is being waived.

Mr. COGHLIN. I think, first of all, sir, we should make clear, as your question correctly has made clear, that this is only one of our concerns.

Mr. LAUGHLIN. And I am asking you to give more than in the line of policy defenses, why is that a problem to you?

Mr. COGHLIN. It really underlines the fact that we are indemnity underwriters behind the shipowner. For us to write a policy for a shipowner we need to be assured of a number of things. Starting with very simple things like that he should describe the ship properly to us when he enters the ship in our club. Secondly, that he will pay his premium to us. But thirdly and most importantly, that he will maintain that ship properly during the time of our policy. And I think this is a very important aspect of what we are talking about here. And I remember having a discussion with your Chairman in November of 1991 in this same room on exactly this issue.

The point really is this, that it is actually in the public policy of the United States that the insurer of ships should retain the policy defenses that relate to the maintenance of the ship for safe trading. Direct action—in which the insurer is suable, regardless, in a direct way and loses, therefore, his policy defenses—takes away from the insurer the one lever he has to compel his insured to maintain his ship and to operate that ship safely; and the safety of the ship, of course, is of direct concern to those who will be damaged if that is not so.

Therefore, it does seem to us that it would not be only normal and natural that policy defenses relating to the safety of the ship should be maintained for a proper relationship between the insurer and his insured, the shipowner, but that it is also consonant with the public policy of any caring state that the ship should be maintained under the threat of the removal by the insurer of his cover if, for example, the ship comes out of class; it has not been inspected as was promised by ABS or ABS has said you should have made this repair or that repair and the shipowner has straightforwardly failed to do that. We all have an interest in the whole system which underlies the enforcement of the safety and proper running of these ships. And the only way the insurer can help you with that is if you let that insurer continue to have those policy defenses. So direct action in this sense is actually the enemy of safe operation of ships.

Mr. LAUGHLIN. Could I interrupt to say this? If you don't have the policy defenses, then the shipowner or ship operator is not required to have any responsibility in the conduct of their business; isn't that true?

Mr. COGHLIN. That is correct.

Mr. LAUGHLIN. And so if you take away the policy defenses, you can have a shipowner out there operating loosey-goosey without any responsible conduct and you and your members are concerned that when that happens you buy the whole farm.

Mr. COGHLIN. That is right. And the whole world is saying to us insurers "you help in this mission to enforce better standards in

the ships at sea." How can we do that if you take away the one lever that we have?

Mr. BRYANT. Congressman, I wonder if I could add a slightly different perspective on that.

Mr. LAUGHLIN. Yes, sir.

Mr. BRYANT. Because you may be asking yourself why, if the P&I Clubs have this strong and sincere belief that they can't rely on the provisions of OPA 90 and the terms of the rule and the wording of the guarantees to protect themselves against unlimited guarantor's liability, why do the Shoreline people actually say they are happy to give the guarantees and happy to rely on those provisions? It does seem to me that at least for the record I should explain what the Shoreline people feel about this.

We would observe that direct action has been the worldwide standard for oil pollution liability since the early 1970's. The international convention regime requires certificates of financial responsibility and direct action. The P&I Clubs have been giving those certificates, those guarantees and responding to direct action, as Mr. Coghlin said this morning, very successfully for 20 years.

Under the Clean Water Act, I think since 1974, the P&I Clubs have actually been giving COFR guarantees, albeit in different form, for lower amounts than those required under OPA. As far as I know, there has not been a single case in 20 years where the COFR guarantee amount has actually been exceeded in the United States. There hasn't been a case where a court has actually broken the guarantor's right to limitation.

The Shoreline managers take at face value what the Coast Guard has said here and what the law has on its face. We don't have any difficulty with it. It seems to us that the question of policy defenses and the question of maintenance of standards is a different question.

There are two contracts involved here. One is the contract for a guarantee to the Coast Guard. And the other is the contract of insurance between the P&I Club and its member.

The contract for insurance between the P&I Club and its member contains policy defenses. And actually Shoreline, just as with the International Group, has the power if, in fact, a shipowner has cheated it or has misrepresented in getting cover or something like that, to recover from that shipowner any amounts that it pays under its direct action. That has been the case in the P&I world forever and a day and it works extremely well.

I have to say with the greatest respect to Mr. Coghlin that I just don't agree that having a direct action standard in oil pollution has any effect on the ability of the P&I Club to maintain standards.

Mr. LAUGHLIN. Well, with your great respect, I do note in the Registrar of Companies' letter to Mr. Tauzin that your company has been incorporated since February the 18th, 19th;, is that correct, the letter?

Mr. BRYANT. That is correct.

Mr. LAUGHLIN. I want to ask you a more direct question that Chairman Tauzin gave me and that was earlier today you testified that your company was more than willing to provide insurance oil spill pollution to the barge traffic and that is one that I had specifically in mind. And Mr. Tauzin also indicated that in your testi-

mony your company would bill on a per trip basis. Am I phrasing what he whispered to me generally?

Mr. BRYANT. I am grateful to have the opportunity because we had the green, yellow and red regime in existence, and I didn't quite manage to get through my speech fast enough this morning.

Mr. LAUGHLIN. As you finish, I want you to also address that if you are going to bill on a per trip basis, shouldn't it be a concern to the barge owner or barge operator that you will change your rate or have the ability or the right to change your rate on a daily basis, depending on many factors, over which a particular barge owner will have no control? Now, I am ready to listen to your completion, if you will address that, also.

Mr. BRYANT. Thank you. Shoreline intends to charge its members rates according to tariffs and those tariffs will differ depending on whether the ship or barge or whatever involved is a tanker or not a tanker. In both cases, cover will be provided on an annual basis from the date of the inception of the cover for a year thereafter.

If it is a nontanker, the tariff will provide for an annual rate and that rate will range between $3,000 and $5,000 a year, based on the size of the ship involved. If it is a tanker, the tariff is more complicated and is intended to fix the cost of the coverage to the parcel of oil actually being carried, so that the shipowner concerned can actually pass this additional cost down to the charterer and the cargo owner so that the cost of this insurance doesn't stick with that shipowner and prove an insupportable burden.

Now, the tariff for tankers provides that the annual coverage is actually paid for on a per voyage basis. The member makes a declaration regularly of the number of voyages he has actually accomplished within United States waters. And if he is trading continuously in U.S. waters, then a period of 30 days is taken to represent one voyage.

Mr. LAUGHLIN. Say that again.

Mr. BRYANT. If he is trading continuously, as say a barge owner trading inland would be, then he pays effectively per month. And unless he can say definitely I have done so many voyages and it is better for him, he pays whatever is best in terms of cost-effectiveness for him on a per voyage basis or a per 30 days basis. He has to pay always with one voyage in hand, which goes back to the point the Chairman is obviously very worried about—a situation where somebody has not paid their premium and, nevertheless, the insurer, the P&I club, is on the hook for payment under direct action and under a guarantee. In Shoreline we have taken steps to make sure that won't happen because you do not get a guarantee given to the Coast Guard unless you have paid in advance and you always have to pay one voyage in hand, as it were, to give a buffer of time. Thus, if the owner starts to default in payment, then Shoreline has time to give the requisite notice to the Coast Guard that they are pulling the guarantee. So, in fact, nonpayment isn't going to be a problem which would be a burden to the rest of the membership.

Mr. LAUGHLIN. And so your rate to—going back to my question, as I understand your answer, the rate is not subject to variation on a day-to-day trip from Houston to——

Mr. BRYANT. No, it will be an annually revised tariff. And the tariff actually goes by a number of different factors. We have asked for the tariffs actually to be included in the record so you can study them.

But basically, they recognize, first of all, the size of the ship involved, in deadweight carrying capacity, the type of the ship—in other words, whether it has any of the proactive, ecologically-friendly features such as a double hull—and the type of oil carried, whether it is a crude oil or light oil product, and finally the age of the ship. It will encourage shipowners to have newer and more ecologically-friendly ships. It will give them an economic reason for doing so.

Mr. LAUGHLIN. Mr. Coghlin, in response to my question about policy defenses, you indicated that was not your only concern. Rather than get you to go through all the concern, if you have already done that earlier in the testimony, my question should be are you satisfied you have gone through your other concerns, other than the policy defense problem in your earlier testimony prior to my arrival or were there others that you felt that you should tell us about?

Mr. COGHLIN. I appreciate your question, sir. I think in our written testimony, both in 1991 and also prepared for this hearing, we have actually touched on each of those concerns. And there is an aggregation of them.

Thank you for the opportunity.

Mr. LAUGHLIN. Thank you very much. Thank you, Mr. Chairman.

Mr. TAUZIN. Thank you, Mr. Laughlin, we have another vote on the Floor. I just want to wrap up this panel if we can. We will take a recess for the vote and come back with the third panel.

I very much appreciate the discussion you had with Mr. Laughlin, Mr. Coghlin, specifically on the concern that if the Coast Guard interprets the law to provide absolute coverage in all cases. This includes whether premiums are paid, whether maintenance is conducted on the vessel, whether the equipment is kept up-to-date and whether class is maintained. They want to make sure that there is always the availability of this coverage regardless. There is a great deal lost in terms of the leverage exercised against shipowners who could lose coverage if they don't properly maintain their vessels and keep their equipment up-to-date.

The reason I wanted to point that out is that one of the findings we made when we examined oil spill problems across this country was that in many cases the problems were not only related to human error, but also very much related to steerage problems and to equipment failures aboard vessels. In many cases, the lack of proper maintenance was directly attributed as a reason for the spill in the first place. That is unfortunate.

If we are to interpret what we have done in OPA 90 is to require such absolute guarantees of coverage by waiver of all policy defenses, that will take responsibility away from the operator of the vessel, we may have made an awful step backwards in the prevention of oil spills. I should hope that that is not the direction these rules take us. But I very much suspect, perhaps, they have.

We will submit some written questions. Mr. Bryant, I particularly want to know a little bit more about the policies of Shoreline

on reinstatement, and about the liability requirement is unlimited for a member to contribute to the funds of the association. We will get into that with written questions.

Mr. BRYANT. It means, Mr. Chairman, exactly what it means in the International Group. It is the same rule that the International Group has.

Mr. TAUZIN. Then, if you have losses, everybody has to chip in to cover the losses. So, a per voyage assessment could be exceeded by the requirements of a contribution if there is a loss.

Mr. BRYANT. But those supplementary calls would be referred back to each voyage.

Mr. TAUZIN. Mr. Youell, we will have a few other questions for you. I particularly wanted to tie down a couple of your comments on the Lloyds of London's testimony. We have about seven minutes left on the vote. We will take a break for the vote, and with my great thanks and appreciation from all the committee for your attendance and patience with us this afternoon. We apologize for the interruptions. We will thank this panel and call the next panel on our reconvening in about 10 minutes. The committee stands recessed.

[Recess.]

Mr. TAUZIN. The hearing will please come to order.

We have some folks who have to catch planes and we are going to have to hurry. We will enforce the light rule.

I know Mr. Law, you have a plane and others.

We welcome this panel and introduce first Mr. Bruce Law, Vice President of the Allied Towing Corporation, Norfolk, Virginia. And I will introduce the remaining panelists as we go forward.

STATEMENT OF BRUCE LAW, EXECUTIVE VICE PRESIDENT, ALLIED TOWING CORPORATION, NORFOLK, VIRGINIA, ON BEHALF OF AMERICAN WATERWAYS OPERATORS; LISA SPEER, SENIOR POLICY ANALYST, NATURAL RESOURCES DEFENSE COUNCIL; MILES KULUKUNDIS, CHAIRMAN, INTERTANKO; AND JERRY A. ASPLAND, PRESIDENT, ARCO MARINE, INCORPORATED, ON BEHALF OF AMERICAN PETROLEUM INSTITUTE

STATEMENT OF BRUCE LAW

Mr. LAW. Good afternoon, Chairman Tauzin and Members of the subcommittee. My name is Bruce Law, and I am Executive Vice President of Allied Towing Corporation, a Norfolk, Virginia, based transportation company operating 15 tank barges, five of which are dedicated to petroleum transportation, and seven tugboats. Allied Towing is a family owned business which has been in existence since 1956.

I appear here today on behalf of American Waterway Operators. We appreciate the opportunity to appear before you to identify for this committee the impact this rule has on the U.S. towing industry.

We have prepared and submitted more extensive testimony for the record. My remarks this afternoon will focus specifically on the impact of the interim final rule on independent coastal tank barge operators. These are companies like mine who stand to lose the

most if the Coast Guard's financial responsibility rule is implemented as currently drafted.

Mr. Chairman, the implementation of this rule threatens the very existence of the small- to medium-sized coastal companies, which have long played a critical role in the distribution of petroleum in the United States. Perhaps the most pronounced concern of the tank barge industry with respect to the interim final rule is this: We are facing these threatening impacts not because the existing system of providing pollution coverage in this country has failed, but rather because the Coast Guard has failed to find a way to incorporate in the financial responsibility regulations a mechanism which allows this time-tested system to continue to function.

For years, many U.S. coastal tank barge operators, including Allied, have obtained protection and indemnification insurance, which includes pollution liability coverage, through the International Group of P&I Clubs. By all accounts, and in my own experience, this system has worked extremely well.

The P&I Clubs have a long history of prompt indemnification of pollution liability claims. Unfortunately, instead of adopting a rule which builds upon this time-tested pollution coverage regime, the Coast Guard would have vessel operators like Allied stake our companies' future on an entirely new system of coverage.

Perversely, what this interim rule does is encourage vessel operators to reduce the level of pollution coverage which they have historically carried, and instead obtain a guaranty of insurance only to meet the OPA-mandated limits, ironically, at much higher rates than vessel operators currently pay today.

This would effectively reduce the financial ability of companies to clean up spills. It would also expose the Oil Spill Liability Trust Fund to a greater financial drain than would occur under the existing regime today.

Let me give you a personal example of the dilemma which companies like mine face. Keep in mind that while self-insurance, provided that a waiver of working capital requirements can be obtained from the Coast Guard, may be an option for the very largest of companies, it is not an option for companies that are small- to medium-sized like ourselves.

For Allied Towing and companies like it, the only real alternative is to find an insurer willing to act as a guarantor for purposes of the financial responsibility requirements under OPA. However, because the insurers upon which we now rely for pollution coverage have said that they cannot act as guarantors, we are faced with a significant—and for some companies an insurmountable—problem of added cost. I cannot accept that it was Congress' intent to drive small, responsible companies like ours out of the oil and chemical transportation business.

Allow me to illustrate one fact. For the 1994–1995 policy year, Allied anticipates paying just under $1 million for liability coverage for our international P&I Club. In addition to the standard protection and indemnification coverage that that policy provides, it also includes oil pollution liability coverage of up to $500 million per incident, plus $1 billion of coverage for any other type of incident, including hazardous chemical spills, and that covers our entire fleet of vessels. Under the interim final rule, however, this coverage can-

not be used to satisfy my company's COFR requirements for 10 million for oil pollution coverage and the additional 5 million required for hazardous substance spill coverage.

For that, we will have to obtain an insurance guaranty from an entity such as the proposed Shoreline Mutual Limited, a Bermuda-based company, assuming that they are able to obtain reinsurance and become a viable operation. Using Shoreline's draft tariffs provided to me in June of this year, to supply a COFR covering just my five dedicated oil tank barges will cost Allied Towing $1,851,479 annually, and that is solely for pollution coverage, no protection and indemnification coverage at all.

This means our insurance expenses in this area will more than triple, while the level of my pollution insurance coverage will decrease to just 2 percent of its current level.

Even if my company could afford the substantial increase in cost, this massive decrease in this pollution liability coverage is something that neither I nor my shipper customers can accept. Operating oil and chemical barges with just 15 million of pollution coverage for oil and hazardous substances clearly endangers the viability of Allied Towing. It also——

[The statement of Mr. Law may be found at end of hearing.]

Mr. TAUZIN. The time has expired, Mr. Law, and I am going—we are going to get right into questions for you so that you can get out of here.

You just hit the point that I think is most cogent in your testimony. If I get your numbers right, you now have P&I coverage at a cost of $1 million?

Mr. LAW. Approximately, sir.

Mr. TAUZIN. That covers you for $500 million per incident and a billion dollars of coverage for other types of incidents including hazardous substance spills for the entire fleet.

Mr. LAW. Yes, sir.

Mr. TAUZIN. Now, because of these new rules you are going to have to deal with a new entity that is going to cost $2 million for five of your tank barges and will only give you $10 million of coverage.

Mr. LAW. My understanding is that is correct, 1.8 million.

Mr. TAUZIN. I thought these rules were to improve the security of insurance for oil spills in America. If my math is right, to get $500 million of coverage, at $2 million for 10, it would cost you $100 million under the new regime. I doubt seriously that you could sustain that obligation anywhere.

Mr. LAW. That is certainly our fear.

Mr. TAUZIN. You make a point that your company is not capable of meeting the self-insurance provisions. Are there any of the other options that you could meet other than buying this new insurance if it is available?

Mr. LAW. All the options that we have investigated, we have come up with nothing.

Mr. TAUZIN. So, if the Coast Guard COFR rules stay in effect as it has been promulgated, and if you are left with the only choice of using one of these new insurance forms described to us today, you will be left with less coverage at a much higher rate without

the availability of availing yourself of any other option other than what you have described to us here?

Mr. LAW. That is the way it stands today, yes, sir.

Mr. TAUZIN. What is likely going to happen to your company under those circumstances?

Mr. LAW. My crystal ball is rather cloudy today. I could easily stop operation come July 1st, 1995.

Mr. TAUZIN. If there is a spill, is it pretty certain that you would not have the coverage anymore?

Mr. LAW. Not that I would be satisfied with or comfortable with.

Mr. TAUZIN. I understand Mr. Kulukundis—same name, but not related—also has a flight. Therefore, I am going to try to pass on any questions to Mr. Law first.

Mr. Gilchrest, do you have any questions?

Mr. Law, we thank you, your testimony is quite specific and good and we appreciate it. And if you do have to make that flight, we appreciate it and would be glad dismiss you at this time.

We will call on you Mr. Kulukundis because I think that you have a flight scheduled.

STATEMENT OF MILES KULUKUNDIS

Mr. MILES KULUKUNDIS. Thank you for the opportunity to appear before you today. I am Miles Kulukundis of the International Association of Independent Tanker Owners, INTERTANKO.

INTERTANKO's members face an immediate crisis in finding means of complying with this new rule. We and potential claimants in the United States also appear to be on the verge of losing the benefits of a proven cost-effective system for handling pollution claims. I am speaking of the international group of protection indemnity clubs that have operated successfully in the United States and around the world for a century.

The Coast Guard's rule requires compliance using methods that are available only to a small proportion of the tanker fleet serving the United States. For the overwhelming majority of the tanker owners, self-insurance and a surety of the requirements cannot be met. No other means of compliance has been developed to the point of approval by the Coast Guard.

The Coast Guard has nonetheless placed great reliance on the emergence of alternatives to P&I certification. These alternatives, whatever their ultimate merits, are purposely built solely to provide a structure that conforms to the Coast Guard's rule. They have no history of operation, and no one can at this point know whether these alternatives are viable guarantors.

This brings me to the question of the role of the P&I Clubs. These Clubs have historically provided a high level of protection at low cost. They have been reliable and efficient.

The Clubs have stood by their insured and provided prompt payment to claimants. At a time when we are all concerned about the rapid response to environmental mishaps, are we prepared to forgo the proven capability of the P&I Club's involvement in U.S. maritime pollution protection?

We are prepared to consider and discuss means of compliance with any party that has a reasonable suggestion. However, we urge

Congress to ensure that any solution to this problem accommodates the P&I system and its capabilities.

I thank you, Mr. Chairman, and I would be happy to answer any questions that you may have. And I do have an amount of time, so I am quite happy to stay until the end of presentation.

Mr. TAUZIN. We appreciate that.

I thought you had a 3:30 flight.

[The statement of Mr. Miles Kulukundis may be found at end of hearing.]

STATEMENT OF LISA SPEER

Mr. TAUZIN. We will now hear from Ms. Lisa Speer, Senior Policy Analyst from the Natural Resources Defense Council.

Ms. SPEER. I wanted to start by emphasizing the importance of the financial responsibility rules. The fundamental principle at the heart of OPA is the principle that the spiller should pay for oil spills and that principle rests on the twin pillars of higher liability limits and requirements that potential spillers demonstrate that they have the financial wherewithal to pay for a spill up to the liability limits.

Financial responsibility rules are crucial to ensuring that this fundamental principle of OPA is implemented. And they also provide strong financial incentives to prevent spills and to help discourage fly-by-night operators.

Prompt implementation of these rules is important because certain preexisting financial responsibility rules will remain in effect until the Coast Guard's rules become final. Those preexisting rules offer levels of financial responsibility at levels far lower than those required by OPA. And even with a small spill those levels of financial responsibility could easily be wiped out. For these reasons, it is crucial that these financial responsibility rules, in our view, be implemented as rapidly as possible.

The industry has raised a number of objections, which I would like to address briefly. Most of these objections appear to have more to do with OPA than with the financial responsibility rules.

And I wanted to address these provisions of OPA because they were considered by the Congress in great detail and were passed unanimously in 1990. The first is the concept of direct action against a guarantor. Direct action is really a crucial component of the principle that the spiller should pay for oil spills.

Financial responsibility provided by a guarantor without an underlying right of action against that guarantor is not an enforceable assurance of financial responsibility. This concept is not a new concept, as previous witnesses have noted. It has been around for a long time. It is incorporated into most pre-OPA statutes and in the international regime.

The second section—provision of OPA that has been objected to is the concept that States are not preempted from their own liability laws. State preemption would prohibit States like Alaska in the Exxon Valdez case or New York from joining together with the Federal Government to recover damages for natural resources. And that is why State preemption received strong support from the Congress—no State preemption received strong support from Congress.

With respect to the liability limits in OPA, there is evidence that they are low, not too high. The cleanup costs in the Puerto Rico barge spill that happened in January of this year, topped $20 million, which is twice the OPA liability limit and 25 times the financial responsibility guarantee provided under the Clean Water Act, in the first 10 days of the spill.

Right now, cleanup and damages, not including damages to natural resources which have not yet been assessed, now stand at, roughly, $100 million. That is 10 times the OPA liability faced by the vessel, assuming that liability was not broken.

Some have argued that guarantors face unlimited liability under OPA and we have heard these fears expressed here today by a number of witnesses. The statutory limits on liability are exceedingly clear in the statute and it is very clear that the guarantor's liabilities cannot exceed those limits. The Coast Guard has erected additional protections and the implications that U.S. courts will somehow ignore the statute and the rules, I think, are unfounded.

The proposal that has come out of the industry for P&I Club membership is an asset, the purpose of this appears to be to allow the P&I Clubs to avoid direct action, and that, in our view, would completely undermine the concept that the spiller should pay because the P&I Clubs could invoke their policy defenses to avoid payment. It would be in clear contravention of the purposes of OPA and we feel it was properly rejected by the Coast Guard.

Finally, to briefly address the train wreck, dire warnings are being sounded from a lot of different quarters about the train wreck. Under this scenario, the P&I Clubs will refuse to act as guarantors, no other option will be available, oil transport to the United States will cease, and the economy will collapse. We do not think this scenario is credible for a couple of reasons:

First, the P&I Clubs are controlled by their membership owners and operators. The ideas that these shipowners and operators are powerless to control the actions of the P&I Clubs is not credible.

Second, similarly dire predictions were made in the debate over OPA that vessels would stop serving U.S. ports as a result of the liability regime imposed here. But according to a study done by DOE, all of those threats were empty; virtually all independent tanker companies remain in the United States market, and the vast majority of oil companies are committed to maintaining or expanding their fleets.

Finally, U.S. trade accounts for one-third of all world seaborne oil movements. And the likelihood that the oil companies would abandon the U.S. market rather than to order the P&I Clubs to revise their policy is not credible. And if they did, alternative financial responsibility resources are available, as previous witnesses have indicated.

The Coast Guard's approach is legally sound, fiscally prudent, environmentally appropriate and long overdue. We strongly support it.

Thank you.

Mr. TAUZIN. Thank you.

[The statement of Ms. Speer may be found at end of hearing.]

Mr. TAUZIN. And finally, Mr. Jerry Aspland, President of ARCO Marine Incorporated, representing the American Petroleum Institute.

STATEMENT OF JERRY A. ASPLAND

Mr. ASPLAND. Thank you.

My name is Jerry Aspland, Chairman of the API Tanker Transportation Committee and President of ARCO Marine. With me I have two colleagues, an independent shipowner, Mr. Charles Kurz from Keystone Shipping, and a major charterer, Mr. John Eller, Shell Oil Company.

I am not going do read my testimony, but I am going to start out with some recommendations for the committee.

Your committee should request the Coast Guard to make monthly reports to it regarding the progress of the implementation of the rule and the number of applications received and processed.

Number two, the committee must petition the U.S. Coast Guard to supplement the rulemaking with a process to allow more compliance options. I need not go into that any more, because we have heard a lot of this kind of testimony today.

Third, the committee should immediately request the Coast Guard to share with it the criteria for evaluating what qualifies as a financial instrument. The written criteria may provide the key to making progress with this issue.

And what I am saying is that we have been unable to this point in time to get from the Coast Guard just exactly what criteria is necessary to qualify the financial instrument. If we had that, there may be a key.

Concerns of API: A lot has been said about the interruption of crude deliveries in this country. One can develop as many scenarios as one wishes. But we all must remember, the Coast Guard holds all the marbles with this issue, because if interruption begins, the Coast Guard can pull the rule and we can go back to where we are. I do not think that is the way we ought to do this, but there is that option.

Concern number two, and that has been brought up before and that has to do with timing. I am just going to go quickly and say if I was going to fix a ship for December delivery, I would have to do that sometime in October. I would not fix a ship to come to the United States of America in October, pay that fright rate, if I was not sure that in fact that particular ship would have a certificate.

It would be too big of a risk. Not only would I have a ship issue but I would have a ship full of cargo which I had paid for.

Number three, this kind of insurance, what I call the "overcap," is an inefficient use of capital and capital is important to most of us and our members.

As we understand the application of the rule, yet another pot of money or pot of gold is being requested to provide for oil spill cleanup and claims. Presently—let's go down the line: Shipowner's P&I; probably 90 percent of all tankers in the world have $500 million worth of P&I coverage.

Number two, we go to the Federal fund; that is $1 billion. And then let's go to the State funds, and they can vary anywhere from $25 million to $500 million. And there is $2 billion, and all of a

sudden we are going to add another fund with the Coast Guard's number of $415 million.

Well, if I had the $415 million to put in capital, I think I might be able to get a few more jobs in the oil patch, which are important to all of us, instead of giving the money to another level of insurance, if you will, not accomplishing anything, and therefore this money would leave this country. We would not keep it here because it is going to go offshore.

There is some very onerous legal issues, and I have been cringing—and I am not a lawyer but some accuse me of being a lawyer—but when we talk about limits of liabilities and breaking of limits of liabilities, and if you go look at CERCLA and you look at Section 108, and I think that is the right section, it talks about the limits of liability, and I think that is 108(a).

If you read 108(b), it tells you exactly how to break those limits of liabilities, and frankly, I think someone ought to look at it because it is very easy under CERCLA to break the limits of liability, especially if you do not negotiate in bad faith—or you do negotiate in bad faith.

Four, another concern, the Coast Guard is choosing not to allow the utilization of P&I regimes. The committee has already heard testimony about this subject, but I would like to stop a moment and give the committee some information about P&I Clubs. P&I Clubs first are an indemnity organization primarily based in the UK under U.S. law—under English law. Tanker owners make up approximately 10 percent of the membership. We do not have control of those P&I Clubs.

Premium income from tankers range somewhere between 8 and 15 percent, yet the Clubs pay out to this country almost 90 percent of all claims. We ought to think about it before we damn the P&I Clubs.

Two other personal observations; November 4, 1991, I wrote this committee a letter concerning this very subject. I find that today I could have read the same letter and met the requirements of this hearing. It is not a shame that we haven't had at least a teensy-weensy-eensy progress toward solving this issue.

Last, we have been reams and reams of paper and information submitted to this docket. And you know, I just wonder if we couldn't have taken some of that resource and put it toward the solving of the problem. Maybe we are all not seeing the forest from the trees.

[The statement of Mr. Aspland may be found at end of hearing.]

Mr. TAUZIN. Good timing.

Thank you, Mr. Aspland.

We have some time for questions, so you can elaborate if you like in this period.

First of all, Ms. Speer, were you here for the previous panel? Did you hear the discussion of the concern that if you have an absolute guarantee and waive policy defenses, that you are lifting the burden off of the spiller, the operator, to properly maintain, properly supervise his equipment and properly keep it up-to-date and properly class his vessel?

The concern is that under the current P&I system because the shipowner in order to keep his coverage has to meet those require-

ments of maintenance, you have some leverage in the formulation of insurance to ensure compliance; some control over the quality of the ship; and the way it is run, operated, and maintained. The concern is that if you eliminate those defenses and waive them in these rules and always make the insurer responsible, regardless of the activities of the shipper, you are doing the opposite of what the environmental community and I think all of us, wanted to do when we passed OPA 90. I believe we all wanted to put the real onus on the shipper to be more careful and not to spill and be more responsible if a spill did occur. Do you have any comments on that?

Ms. SPEER. Thank you Mr. Tauzin.

I agree that economic incentives are very important component of preventing oil spills. I am not an insurer, but if I were looking at providing a guarantee to a shipowner, then I would want to make certain that that shipowner was operating his or her ship in a proper and safe manner, and I would make sure that no shipowner that was behaving in another way, in a way that was unsafe, would get my guarantee.

So, I think the financial incentive is still going to be there. In other words, in order to get a guarantee from any entity, the shipowner is going to have to demonstrate that they operate safely.

Mr. TAUZIN. That probably is true, that initially before I issue the insurance, I am going to do that inspection. I am going check to make sure that the equipment is there. The concern is that while you are insured, you are operating the vessel for maybe 30 day transits which could be 12 times a year or maybe just six times. I am not sure what the number is during those periods, however, the equipment is going to wear and tear and tire. But during that year the shipper doesn't have to worry because he is always going to be covered.

Haven't we lost an incentive on the part of the shipper to maybe instruct his crew to constantly maintain the vessel during the voyages to ensure that that insurance is always there when he needs it. Under the current system, if he doesn't do that, and fails to maintain, the policy defense can be asserted by the insurer and he ends up holding the bag without insurance. That is, in essence, what I am hearing from Mr. Coghlin.

In essence, the argument we are hearing from the P&I Clubs which seems to have a lot of validity in terms of not the initial insurance but the continuation of maintenance during the insured period while you are at sea is a problem. I doubt seriously that the P&I representatives can constantly visit the ship and look at all the equipment and see how it is working. That is the problem.

Ms. SPEER. Again, I was relieved to hear that you said you were not raised in the realm of insurance law, because I have not been either. But the way that I understood the explanation of the Shoreline representative, and again I may not understand this fully, but that the contract for a guarantee is separate from the contract for the underlying indemnification insurance and that there are still policy defenses there, so that those will continue to operate but not in the context of the guarantee.

Regardless of that question, even if I totally got that wrong, I do believe that there will be substantial incentive for the insurers to have a lot of oversight over tanker vessel operators.

Mr. TAUZIN. I hope you are right. I fear the concern expressed by the P&Is might be correct.

The other question is in regard to direct action. You made the point that the purpose of the OPA 90 was to indeed point the finger of responsibility to the spiller. But the direct action we are talking about is not a spiller. It is the insurer. It is the person who stands behind the spiller, that is the point of contention here.

Ordinarily, if I have to be first responsible, you sue me, I then call my insurer into action behind me. But, you have pointed the finger at me.

The concern expressed here is that with the direct action provisions applied to insurance coverage, as a P&I insurer, that you are literally turning away from the spiller and instead calling on someone who has a contractual obligation with him and not necessarily pointing the finger at the spiller.

In the case of the P&I Clubs, as I understand it, even under Shoreline, you are going to have a continuous responsibility to call upon all the partners or members of the association to come in and bail out this particular spiller. If you provide direct action against all of these people through their association rather than against the spiller, maybe you are pointing the finger at the wrong people again.

My point, I heard today and it continues to bother me, is that if we implement the rule in such a way that the finger is pointed at the financially responsible parties who may not be the spiller, but all the other good shippers, then we may have missed the boat in terms of the way in which OPA 90 is going to work on blue-water fleets.

Ms. SPEER. I think that is a legitimate question to raise. I would have a couple of responses.

First of all, the purpose of direct action is to ensure that there is financial guarantee that there is money out there to pay for a spill so that the public does not end up holding the bag. Presumably, the spiller does pay through the premiums that the spiller pays to the guarantor to obtain insurance coverage, so that there is some cost borne by the spiller.

The purpose of all of this is to ensure that the public does not end up paying for spill cleanup and damages, and that money is available so that that burden does not fall on the U.S. taxpayer.

Mr. TAUZIN. That point is very valid, but I am going to raise this concern. The $1 billion fund that we have collected and we would collect again if it were used as an insurance fund is coming from the oil industry. It is coming from those of us who use the industry.

These new fees are going to come from shippers who are going to charge the oil industry and they are going to charge us for that. I don't understand how we have improved our position when you have added more cost to the provision of protection insurance and it all falls back on us anyhow. That is one of the big question marks I am left with after this hearing today.

What we have done is layer the responsibility, which was more direct prior to this rule and is now going to fall on a new insurance company and all of it passed back to us in the form of higher gasoline taxes which I suspect is going to be more than the Coast Guard's conservative estimate of $415 million. If you heard Mr.

Law's testimony, if he is correct in terms of the new cost for less insurance, I suspect that the number is going to be higher.

Where have we benefited if it is all falling back on the taxpayers and all we have done is add a new layer of insurance. That is what troubles me?

Ms. SPEER. I would respond by using the *Exxon Valdez*. The OSLTF is capped at $1 billion. If the *Exxon Valdez* had been the Joe Blow Shipping, and that spill, the cost of which stands at $3.4 billion right now, would have blown through the OSLTF, and there would be no money left to pay the remaining bills from the *Exxon Valdez*. The U.S. Government would end up footing the bill for that.

Exxon is paying that bill now and presumably some of that, you are right, is probably getting passed through to those of us who consume oil and taxpayers who consume oil, but some of that money is coming out of Exxon's pocket and it should. The way to improve spill prevention in this country is to give very strong financial incentives to companies not to spill oil.

Mr. TAUZIN. Under OPA 90, if it were Joe Blow Oil Company who did not have Exxon's resources and the fund had to be used, the collections automatically kick in. We refill the fund, empty it out. It kicks in again, we refill the fund and pay it out.

I mean, we have literally with OPA 90 funding, provided a mechanism to ensure that the oil companies end up paying for those spills. While none of us can be protected, it isn't going to be passed on to us. I am sure that Exxon has passed on to us what they can already.

The bottom line is that we have provided a mechanism already whether it is Joe Blow Oil Company or Exxon to cover those damages as we assess them and properly define them in court action. What I am asking is in terms of the personal liability, financial responsibility of Joe Blow and Exxon and all the others, has it helped us any to add these new layers when we get less coverage and less security?

If Mr. Laws ends up at $10 million worth of insurance at twice the cost of what he used to get 500 million, what good have we done? We have stressed our billion dollar fund in this case when we didn't need to. I don't want to load this on all of you.

Any of you want to comment on it?

Mr. ASPLAND. I would like Charles Kurz, he has made the calculations similar to Mr. Law.

Mr. TAUZIN. Mr. Law testified for his company that he was currently paying a million dollars to insure his entire fleet at 500 million and a billion for the—he is not here, he is gone. But the point we are referring to is a reference to those added cost for less insurance.

Would you like to elaborate on that?

Identify yourself for the record and jump in.

Mr. KURZ. Charles Kurz, II, Keystone Shipping Philadelphia.

Adding to what Jerry Aspland has said from his statement on behalf of API, and Keystone Shipping Company is a member company of API, it is greatly concerned about the timing, uncertainty and cost of implementing the IFR, and in particular, in research that we have done, taking a look at other alternatives that may be

available in terms of surety bonds or other special-purpose facilities.

There are benefit-added costs above and beyond what we are currently paying. And those costs, as we estimate them to our fleet right now and as are being proposed in certain rating schedules for vessels of the age of ours in our fleet, and the number of voyages that they make into the U.S., we are talking over $4 million for our particular fleet of 10 vessels. And that is just unacceptable to us right now from a financial standpoint, because the next thing we have to do is look to see who is going to pay for that.

Mr. TAUZIN. What are you currently paying as opposed to this 4 million? Is that 4 million more than you are currently paying?

Mr. KURZ. That is correct.

Mr. TAUZIN. Mr. Kulukundis, would you like to chip in here?

Mr. MILES KULUKUNDIS. Yes, I can only agree with what has been said. In our case, we average about $200,000 a year for U.S. oil pollution and if we simply take the Coast Guard's figures, you multiply that by anywhere between four to nine times that amount, so we could be going from $200,000 a year to almost $2 million and that is per vessel. Because we make a large number of voyages to the United States.

Mr. TAUZIN. You see, I am appalled. How can anyone come to a penciled conclusion that this rule is going to only have a $415 million impact on consumers, when you tell me that you are going to go from 200,000 to what?

Mr. MILES KULUKUNDIS. It depends which figure you want to use as the multiplier, but we are paying over 200,000 per vessel. And we have six vessels.

Mr. TAUZIN. So six vessels, and if you are talking about——

Mr. MILES KULUKUNDIS. 1.2 to over $10 million, taking the upper end just us alone.

Mr. TAUZIN. I am getting some numbers that seem to indicate that it is a lot bigger than $415 million.

Mr. MILES KULUKUNDIS. But, Mr. Chairman, picking up on what you said, the actual coverage, the coverage is down, but the other thing which has not been mentioned and emphasized about the P&I Clubs, and we the shipowners consider it to be the most important thing, is that they are fundamentally service organizations. We look to them as service organizations.

They have teams to deal with oil pollution casualties and problems, and if we are to lose that it would be a tragedy to the shipowners and a tragedy to the American people, and we feel very, very strongly about that.

Mr. TAUZIN. Thank you very much, sir.

The gentleman from Maryland, Mr. Gilchrest for questions.

Mr. GILCHREST. I yield to the gentleman from Texas.

Mr. LAUGHLIN. I thank the gentleman.

Ms. Speer, the questions I have for you—I have read Mr. Law's testimony, and I have heard that from a large number of people in my area of the country. And I wonder first, where is the benefit to the American people, one, if these small companies like Mr. Law's, many I represent, just go out of business? Who is going to pick up that?

Secondly, if the P&Is are saying they will not under the circumstances as we know them today, provide the coverage, who is going to provide that other than Shoreline who has been identified here, who has been incorporated or organized since February of this year, and according to the testimony, as I read, has not gotten their reinsurance lined up. So where is the benefit to the American taxpayer if all these things collapse?

Ms. SPEER. Thank you, Mr. Laughlin. I hope I am pronouncing that correctly.

Mr. LAUGHLIN. That is good enough.

Ms. SPEER. First of all, to respond to your first question, I don't feel that I am in the position to assess what the options are for this particular company or the particular amounts that he has cited that would presumably kick in.

Mr. LAUGHLIN. Let me add, there are a lot of companies it—I don't represent Mr. Law or his State. I thought I saw something about Indiana in here. Just to clear it up, I represent Texas and I have companies——

Mr. TAUZIN. And well, I might add.

Mr. LAUGHLIN. He wants something out of me, I can tell.

Mr. TAUZIN. Yes, I do.

Mr. LAUGHLIN. But I have a lot of companies operating in my area out of the Gulf of Mexico that go to Pittsburgh and Indiana and all of those places, and they tell me the same thing that I have read Mr. Law writing here.

Ms. SPEER. Well, the Coast Guard has an implementation schedule that is designed presumably to allow these various options to come forward and get more specifically ironed out, so that the point I raised about the reinsurance contract, the implementation schedule allows time for that to be resolved.

Secondly, my understanding is that the Coast Guard has identified other options besides Shoreline that remain possibilities, including surety bonds, and at least one other company, First Line. Now, I am not in a position to be able to evaluate the adequacy of those options, but the Coast Guard appears to believe that those are viable and reasonable options that should be allowed to go forward.

Mr. LAUGHLIN. Let me take you down the coast of Texas where in my district we have a very famous wildlife refuge for the whooping crane, and the barges go through there on a daily basis and have a wonderful relationship with the Fish and Wildlife Service.

If we have an oil spill there, who is going to have the money under your scenario to clean this up if the P&Is are not going to be involved?

And I put it to you this way; with the possibilities of others being out there, when today we are dealing with the certainty of the P&I Clubs and with its track record and with the owners, and we have heard more than one, and I just rely on Mr. Law's written statement and people from my district saying that with certainty they have been there to provide the protection—and it looks to me like what we are trying to do is drive certainty out and bring possibilities in. Which again, I go to you and ask what is the benefit to the American taxpayer, and to use your word, when you talked about

the P&Is on credibility, where is the credibility for the possibilities of Shoreline?

Ms. SPEER. Well, Mr. Laughlin, I would respond in a couple of ways. First of all, the other options that have been identified, the whole project does not rest on Shoreline Mutual. There are——

Mr. LAUGHLIN. Shoreline-types, with no track record in this field, isn't that true?

Ms. SPEER. I am not qualified to answer that question.

Mr. LAUGHLIN. You are here telling us that is a good deal for the taxpayers, and that is the reason I want to know where is the benefit and the good deal for the taxpayers?

Ms. SPEER. Because this rule provides assurance that money will be available to clean up an oil spill should one happen near your national wildlife refuge.

Mr. LAUGHLIN. Where is the certainty if the P&Is are gone? And they tell us they are gone under the rules as we have them today.

Ms. SPEER. The Coast Guard will not accept a COFR guarantee from a company that is not capable of providing that guarantee, I would assume.

Mr. LAUGHLIN. Where is Mr. Law's and, my similar-type companies a thousand miles a way from Mr. Law's, going to get protection to stay in business in the undesirable event that they have an oil spill problem?

Ms. SPEER. I would say, let this rule go forward. Let those companies get themselves and their proposals together and allow them to provide the kind of alternatives that the Coast Guard has analyzed and put forward.

I understand that there is a lot of concern and a lot of fear out there that insurance coverage will not be available. The last thing that we want to see is no insurance coverage available, because the guarantee is the only way that we can be sure that money is available to clean up and pay for damages. We believe that——

Mr. LAUGHLIN. Guarantees of insurance or making the P&Is guarantors?

Ms. SPEER. COFR guarantee is the—a guarantee that makes certain that the money is available; does not use the P&I Clubs because of their policy defenses. If you were to allow the P&I Club membership to be used as an option, and the P&I Clubs exercised their policy defenses, there is no guarantee the money would be there.

So if you had an oil spill off your coast in that national wildlife refuge, you would not have the money. The money would not be there to clean up the spill, and that contradicts the fundamental premise of OPA, that the spiller should pay.

Mr. TAUZIN. Mr. Laughlin, we have about three minutes.

Mr. Gilchrest wants to get in a couple of questions.

Mr. LAUGHLIN. I yield back.

Mr. TAUZIN. Mr. Gilchrest.

Mr. GILCHREST. Mr. Aspland, you made a comment that—and then I am going to ask you to make a quick statement, because this question is actually for Ms. Speers.

You made a comment that the oil tanker or the shipowners make up 10 percent of the P&I Clubs.

Mr. ASPLAND. Correct.

Mr. GILCHREST. And premiums from the U.S. are 15 percent of what P&I gets on a global scale.

Mr. ASPLAND. That is approximately correct.

Mr. GILCHREST. But 90 percent of the claims are directed from the United States.

Mr. ASPLAND. That is my understanding.

Mr. GILCHREST. And Ms. Speer, you made a comment that P&I Clubs are controlled by the member shipowners and operators who elect their directors, and the notion that vessel owners and operators are powerless to influence the position of the Clubs is not credible. Based on the fact that 10 percent of the P&I Clubs are made up of shipowners——

Mr. ASPLAND. Tanker owners.

Mr. GILCHREST. Tanker owners, you say it is not credible to say that the tanker owners don't have influence over P&I. Based on this statistic from Mr. Aspland, could you tell us how that is still true?

Ms. SPEER. Well, it seems to me, first of all, that a 10 percent ownership is a substantial ownership, and I would just ask does that figure include all of the vessels that would be subject to OPA? 10 percent?

Mr. ASPLAND. The number then would probably go down, because that is a worldwide number. It would go down. Got to remember that all P&I Clubs is worldwide coverage, so you have people from all different nationalities in that and national flags, and they do not necessarily come here. So when you have a call, then that applies to everyone.

Very quickly, our insurance rate at my company went up about two years ago. It has absolutely nothing to do with tankers. It had to do with bulk carriers. And because of the losses, we had to make up the difference. And it doesn't have anything to do with us. And my point is that it is in these kinds of regimes, you have to look at the whole picture. And to make a statement that we can control the Clubs, is an inaccurate statement, we cannot.

Mr. GILCHREST. Ms. Speer, do you disagree.

Ms. SPEER. Well, I would say that certainly the shipowners have a substantial say in the operation of the P&I Clubs, and furthermore, the P&I Club option is again not the only option out there. There are other options that are available.

Mr. GILCHREST. Thank you, Mr. Chairman.

Mr. TAUZIN. I would point out to you, Mr. Gilchrest, that the Republicans operate with more than 10 percent of the House. I don't think you are satisfied with your control of the House at this point.

Mr. Laughlin.

Mr. LAUGHLIN. I wanted to say to Ms. Speer, I don't care personally if the P&I Clubs disappear, if we have someone to substitute at greater benefit to the American people, at the kind of coverage that they are protecting, at the prices rather than the reverse.

And I don't mean to pick on Shoreline. I don't care if it is the Texas Farm Bureau providing the insurance, if we are getting maximum coverage and at lower cost for the operator, who in time, if we have a catastrophic event, it is we, the citizens, that need the coverage.

And I don't see the benefit to we, the citizens, if we have double the premium costs and substantially reduced coverage amounts. And that is where I am coming from.

And if you want to be a part and we need to be a part of running off the P&I Club operations, so be it; if we have a substitute to put in there that will provide the same insurance protection at a lower cost.

Mr. TAUZIN. That is going to have to be the last word. We have three minutes for a vote.

I do want to thank you for your participation and all of you for your contributions today. We will be submitting written questions to all of you.

Mr. Bryant, I will want to know the specific reinsurers who have indicated interest and their intent to participate. We will also take those considerations under advisement, Mr. Aspland, as far as your suggestions to the committee.

[The information may be found at end of hearing.]

Mr. TAUZIN. Thank you all very much.

I again apologize. Thanks for your patience. This has been a good set of hearings today.

We appreciate your involvement.

The hearing stands adjourned.

[Whereupon, at 3:55 p.m., the Subcommittee was adjourned; and the following was submitted for the record:]

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DEPARTMENT OF TRANSPORTATION

U. S. COAST GUARD

STATEMENT OF ADMIRAL ROBERT E. KRAMEK

ON CERTIFICATES OF FINANCIAL RESPONSIBILITY FOR

WATER POLLUTION (VESSELS)

BEFORE THE

SUBCOMMITTEE ON COAST GUARD AND NAVIGATION

COMMITTEE ON MERCHANT MARINE AND FISHERIES

HOUSE OF REPRESENTATIVES

JULY 21, 1994

Admiral Robert E. Kramek
Commandant
United States Coast Guard

Admiral Robert E. Kramek is the 20th Commandant of the United States Coast Guard. He is both a Surface Operations Specialist and Naval Engineer with extensive service in all CG regions including the Atlantic, Pacific, Caribbean and Alaska.

Admiral Kramek's previous assignments include Chief of Staff of the U.S. Coast Guard and command of two Coast Guard Districts, the 13th District in the Pacific Northwest and the 7th District in the Southeast U. S. and Caribbean. He has also commanded the Coast Guard Base at Governors Island, New York; commanded the High Endurance Cutter MIDGETT and the Haitian Migration Task Force where he led the interdiction and rescue of 37,000 Haitians. At the same time he was also the Drug Czar's Coordinator for the War on Drugs in the Southeast U. S. and Caribbean. He served as Regional Emergency Transportation Coordinator (RETCO) for the Secretary of Transportation in the Pacific Northwest. He also commanded Maritime Defense Zone sectors Pacific Northwest and Sector 7 Southeast U. S. which are Navy Coastal Defense Commands.

He graduated with honors, from the USCG Academy with a B.S. in Engineering in 1961. Admiral Kramek attended post graduate schools at the University of Michigan, Johns Hopkins University and the University of Alaska. He has received Master of Science Degrees in Naval Architecture and Marine Engineering, Mechanical Engineering and Engineering Management. He also attended the U.S. Naval War College in Newport, RI and graduated with Highest Distinction. Admiral Kramek was selected for Flag rank in 1986. After selection for Flag rank he completed the "Capstone" Program at the National Defense University Institute of Higher Defense Studies.

The Admiral's awards include two CG Distinguished Service Medals, two Legion of Merit awards, the Meritorious Service Medal, four CG Commendation Medals, the CG Achievement Medal, CG Unit Commendations, the Meritorious Unit Commendation, the Special Operations Ribbon with silver star, the Humanitarian Service Medal with bronze star, and the Sea Service Ribbon with bronze star.

Admiral Kramek is a physical fitness enthusiast. He is married to the former Patricia Havard of Washington, DC. They have four children: Tracy, Joseph, Suzanne, and Nancy.

DEPARTMENT OF TRANSPORTATION

U. S. COAST GUARD

STATEMENT OF ADMIRAL ROBERT E. KRAMEK

ON THE INTERIM FINAL RULE FOR VESSEL CERTIFICATES

OF FINANCIAL RESPONSIBILITY

BEFORE THE

SUBCOMMITTEE ON COAST GUARD AND NAVIGATION

COMMITTEE ON MERCHANT MARINE AND FISHERIES

HOUSE OF REPRESENTATIVES

JULY 21, 1994

GOOD MORNING, MR. CHAIRMAN. IT IS MY PLEASURE TO BE HERE THIS MORNING TO ADDRESS THE INTERIM FINAL RULE FOR CERTIFICATES OF FINANCIAL RESPONSIBILITY (COFRS). I AM PLEASED TO REPORT THAT THE COAST GUARD HAS PUBLISHED AN INTERIM FINAL RULE IMPLEMENTING THE VESSEL FINANCIAL RESPONSIBILITY PROVISIONS OF THE OIL POLLUTION ACT OF 1990 (OPA 90) AND THE COMPREHENSIVE ENVIRONMENTAL RESPONSE, COMPENSATION, AND LIABILITY ACT (CERCLA). I BELIEVE THE RULE IMPLEMENTS THE LAW AS INTENDED BY CONGRESS AND BALANCES THE INTERESTS OF UNITED STATES CITIZENS AND THE MARITIME INDUSTRY. THIS RULE HAS SUPPORT BEYOND THE ADMINISTRATION, AND I EXPECT YOU WILL HEAR FROM SOME OF THOSE SUPPORTERS TODAY.

AFTER THE EXXON VALDEZ TRAGEDY IN 1989, OPA 90 WAS ENACTED BY CONGRESS AND SIGNED INTO LAW ON AUGUST 18, 1990. THE LIABILITY AND COMPENSATION PROVISIONS OF OPA 90, HOWEVER, HAD BEEN UNDER DEVELOPMENT FOR MANY YEARS PRIOR TO THAT DATE. DESPITE OBJECTIONS BY THE INTERNATIONAL MARITIME INDUSTRY TO THE PROPOSED LAW'S LIABILITY AND COMPENSATION PROVISIONS, CONGRESS

UNANIMOUSLY ADOPTED A LIABILITY AND COMPENSATION REGIME BASED ON THE FUNDAMENTAL PRECEPT THAT THE POLLUTER PAYS FOR REMOVAL COSTS AND DAMAGES. IN THE CASE OF AN ACCIDENTAL SPILL, THE POLLUTER'S LIABILITY IS LIMITED TO SPECIFIED AMOUNTS, EXCEPT WHERE CERTAIN ACTS OF THE POLLUTER CAUSE THE INCIDENT OR WHEN THE POLLUTER FAILS OR REFUSES TO CARRY OUT HIS/HER RESPONSIBILITIES AFTER THE INCIDENT. WHERE SUCH ACTS OR FAILURES OCCUR, THE POLLUTER MAY BE LIABLE FOR THE FULL COSTS AND DAMAGES (SO-CALLED UNLIMITED LIABILITY).

AS AN ESSENTIAL COMPONENT OF THIS REGIME, CONGRESS RETAINED THE TIME-TESTED CONCEPT OF GUARANTIED FINANCIAL RESPONSIBILITY UP TO SPECIFIED LIMITS, WITH THE RIGHT OF DIRECT ACTION. IN SEPTEMBER, 1991, THE COAST GUARD PROPOSED A RULE TO IMPLEMENT OPA 90'S AND CERCLA'S FINANCIAL RESPONSIBILITY MANDATES, BUT WAS IMMEDIATELY CHALLENGED BY THE INTERNATIONAL SHIPPING INDUSTRY FOR FAILING TO USE THE RULE TO INSULATE THAT INDUSTRY FROM THE POTENTIAL FOR UNLIMITED LIABILITY. THE INDUSTRY DEBATE CONTINUED FOR ALMOST THREE MORE YEARS, BUT OPA 90 WAS NOT ALTERED TO AUTHORIZE THE COAST GUARD TO INSULATE THE SHIPPING INDUSTRY FROM THE POSSIBILITY OF UNLIMITED LIABILITY. ACCORDINGLY, ON JULY 1, 1994, THE COAST GUARD PROMULGATED THE RULE. IT IS THE COAST GUARD'S SINCERE HOPE AND BELIEF THAT NOW THAT THE COFR RULE HAS BEEN ADOPTED, RHETORIC DESIGNED TO CONFUSE FINANCIAL RESPONSIBILITY WITH UNLIMITED LIABILITY WILL BE PUT ASIDE, AND ALL PARTIES WILL TURN TO THE BUSINESS OF COMPLYING WITH THE NEW RULE.

THE CONTROVERSY SURROUNDING THIS RULEMAKING ARISES FROM THE COMMINGLING OF TWO SEPARATE ISSUES: FINANCIAL RESPONSIBILITY AND

UNLIMITED LIABILITY. INDUSTRY'S DISSATISFACTION WITH OPA 90, AS EXPRESSED DURING THE RULEMAKING, HAS BEEN ONE OF THE MOST WIDELY REPORTED MATTERS IN THE DOMESTIC AND INTERNATIONAL MARITIME PRESS, AND HAS BEEN THE SUBJECT OF INNUMERABLE SEMINARS AND CONFERENCES. IN THE CONTEXT OF THE RULEMAKING, THE CONTROVERSY IN SIMPLE TERMS AROSE FROM THE STATED REFUSAL OF THE PROTECTION AND INDEMNITY (P&I) CLUBS, WHICH ARE COMPRISED OF THE SHIPOWNERS THEMSELVES, THAT ARE MEMBERS OF THE INTERNATIONAL GROUP OF P&I CLUBS TO PROVIDE THE INSURANCE GUARANTIES REQUIRED BY OPA 90. THESE SAME P&I CLUBS HAVE PROVIDED OIL POLLUTION GUARANTIES UNDER U.S. LAWS SINCE 1970, AND TO OTHER GOVERNMENTS UNDER INTERNATIONAL TREATY SINCE 1975. SHIPPING INTERESTS STATED THAT WITHOUT P&I CLUB GUARANTIES, THERE WOULD BE NO OTHER SOURCES FOR OBTAINING FINANCIAL RESPONSIBILITY GUARANTIES AND MARITIME TRADE TO THE UNITED STATES WOULD THEREFORE CEASE-- THE SO-CALLED "TRAIN-WRECK." TODAY I REITERATE THE COAST GUARD'S BELIEF THAT THE NEW COFR RULE WILL NOT RESULT IN A TRAIN-WRECK, DESPITE A VIEW BY SOME IN INDUSTRY THAT ONLY A TRAIN-WRECK WILL FORCE CONGRESS TO AMEND OPA 90 OR ABANDON THE POTENTIAL FOR UNLIMITED LIABILITY IN CASES OF FAULT, IN FAVOR OF THE INTERNATIONAL TREATY.

I HAVE APPENDED TO MY STATEMENT A COPY OF THE COAST GUARD'S PRESS RELEASE AND FACT SHEET EXPLAINING THE NEW RULE. ALLOW ME TO BRIEFLY SUMMARIZE IT. THIS RULE IMPLEMENTS OPA 90'S AND CERCLA'S MANDATE TO PROTECT U.S. TAXPAYERS. IT DOES THIS BY ENHANCING THE ABILITY OF CLAIMANTS TO OBTAIN COMPENSATION FOR REMOVAL COSTS AND DAMAGES SUFFERED AS A RESULT OF AN OIL SPILL OR

HAZARDOUS SUBSTANCE RELEASE, DIRECTLY FROM THE POLLUTER OR THE POLLUTER'S GUARANTOR. THE RULE ESSENTIALLY ADOPTS THE THEMES OF THE NPRM, BUT MAKES A NUMBER OF TECHNICAL IMPROVEMENTS IN RESPONSE TO COMMENTS. IT ENHANCES THE STATUTORY PROTECTIONS AFFORDED GUARANTORS. IT PHASES IN COMPLIANCE. IT PERMITS FINANCIAL RESPONSIBILITY TO BE DEMONSTRATED THROUGH THE TIME-TESTED METHODS OF SELF-INSURANCE, GUARANTIES OF INSURANCE OR SURETY BONDS, OR FINANCIAL GUARANTIES. IT ALSO PERMITS A CATCHALL "OTHER EVIDENCE" GUARANTY, AS I WILL EXPLAIN SHORTLY. MOST IMPORTANTLY, IT PERMITS SHIPOWNERS AND OPERATORS TO PROCURE FINANCIAL RESPONSIBILITY IN THE MANNER CONTEMPLATED BY OPA 90'S REQUIREMENTS.

WE HAVE ADOPTED AN INTERIM FINAL RULE WITH A REQUEST FOR COMMENTS. THE 90-DAY COMMENT PERIOD CLOSES SEPTEMBER 29TH. NEVERTHELESS, AN INTERIM RULE IS STILL A FINAL RULE. COMPLIANCE IS REQUIRED. WE SOLICITED FURTHER COMMENTS FOR FINE-TUNING OF THE TECHNICAL ADJUSTMENTS, IF NECESSARY. WE DISCOURAGE COMMENTS ON THE OLD ISSUES, WHICH ALREADY HAVE BEEN DEBATED. THE PURPOSE OF THE COMMENT PERIOD IS TO ENSURE THAT FROM A TECHNICAL STANDPOINT THE RULE IS AS PRECISE AND BURDEN-FREE AS IT CAN REASONABLY BE.

THE MAJOR COMMENTS PROVIDED TO THE COAST GUARD RELATED TO THE OCEAN-GOING FLEET PRESENTLY INSURED BY THE P&I CLUBS. (THE INLAND AND SMALL-VESSEL COASTAL FLEET HAS GENERALLY BEEN WELL-SERVED BY THE WATER QUALITY INSURANCE SYNDICATE (WQIS), AND WE EXPECT THAT RELATIONSHIP TO CONTINUE). AS TO THE MAJOR COMMENTS, THE COAST GUARD REJECTED THE PROPOSAL TO ACCEPT MEMBERSHIP IN A

P&I CLUB AS A FORM OF SELF-INSURANCE. THIS PROPOSAL HAD TWO FORMS-- ONE, MEMBERSHIP CONSTITUTES AN ASSET IN THE SELF-INSURANCE FORMULA; AND TWO, IN ADDITION TO MEMBERSHIP, A MEMBER OF THE P&I CLUB WOULD ASSIGN ITS RIGHTS UNDER THE POLICY TO THE OIL SPILL LIABILITY TRUST FUND (OSLTF) (THE LATTER WAS CALLED THE "LOSS-PAYEE" VERSION). THE COAST GUARD REJECTED THESE CONCEPTS FOR A NUMBER OF REASONS, PRIMARILY BECAUSE THE CONCEPTS DID NOT ACCORD WITH OPA 90. OBVIOUSLY, THE AMOUNT OF AN INSURANCE POLICY, ESPECIALLY AN INDEMNITY POLICY, IS NOT AN ASSET UNDER ANY KNOWN ACCOUNTING PRINCIPLES. CLAIMANTS WOULD HAVE NO ASSURANCE OF PAYMENT SINCE ALL POLICY DEFENSES, SUCH AS A MEMBER'S INSOLVENCY, COULD BE INVOKED BY THE CLUB. THE LOSS-PAYEE VARIATION ADDED NO FURTHER ASSURANCE THAT A CLAIMANT, INCLUDING THE OSLTF, WOULD BE PAID. THESE CONCEPTS INVOLVED NO HINT OF A GUARANTY AND MERELY WOULD SHIFT THE BURDEN TO U.S. CONSUMERS AND TAXPAYERS, THE DIRECT OPPOSITE OF CONGRESS' INTENT IN OPA 90.

ACCORDINGLY, THE METHODS AVAILABLE TO DEMONSTRATE FINANCIAL RESPONSIBILITY ARE THOSE ENUMERATED IN THE NPRM -- SELF-INSURANCE, INSURANCE GUARANTIES, SURETY BOND GUARANTIES, AND FINANCIAL GUARANTIES. AT THE REQUEST OF COMMENTERS, AN ADDITIONAL AVENUE OF COMPLIANCE WAS ADDED -- "OTHER EVIDENCE." AN OTHER EVIDENCE PROVIDER IS A GUARANTOR UNDER THE DEFINITION IN OPA 90 AND, THEREFORE, SUBJECT TO DIRECT ACTION. A LETTER OF CREDIT IN THE PROPER FORM, FOR EXAMPLE, COULD BE PROPOSED AS AN "OTHER EVIDENCE" METHOD. THE "OTHER EVIDENCE" METHOD IS NOT INTENDED TO MIRROR STATE LAWS THAT ALLOW MEMBERSHIP IN A P&I CLUB TO BE CONSIDERED "OTHER EVIDENCE" UNDER STATE LAW, WITHOUT DIRECT

ACTION. STATE LAWS ARE FUNDAMENTALLY DIFFERENT FROM OPA 90 -- THEY DO NOT DEFINE A GUARANTOR THE WAY OPA 90 DOES. MOREOVER, IF A RESPONSIBLE PARTY OR INSURER DOES NOT PAY, OR CANNOT KEEP ITS PROMISE TO PAY, UNDER STATE LAW, THE STATE KNOWS THAT THE FEDERAL OSLTF CAN PROVIDE COMPENSATION. THE OSLTF HAS NO SIMILAR BACK-UP. ONE STATE, WASHINGTON, HAS TAKEN AWAY THIS APPARENT BENEFIT FOR TANKERS AS IT REQUIRES TANKERS UNDER A STATE OIL SPILL PREVENTION PLAN TO ESTABLISH COMPLIANCE WITH THE FEDERAL FINANCIAL RESPONSIBILITY LAW.

OUR RULE DOES NOT PREVENT A P&I CLUB, SHOULD IT ELECT TO BECOME A FINANCIAL RESPONSIBILITY PROVIDER, FROM ISSUING AN INSURANCE GUARANTY. ANY ACCEPTABLE P&I CLUBS WILLING TO EXECUTE THE INSURANCE GUARANTY FORM ARE CERTAINLY WELCOMED AS GUARANTORS, AS THEY HAVE BEEN FOR MANY YEARS. WHETHER OR NOT THE CLUBS' PRIMARY REINSURER, LLOYD'S, WILL PERMIT THE CLUBS TO ISSUE OPA 90 GUARANTIES UNDER THE CURRENT REINSURANCE CONTRACT, I DO NOT KNOW.

AN ISSUE OFTEN RAISED IN THE CONTEXT OF THE RULEMAKING WAS THE ASSERTION THAT GUARANTORS ARE SUBJECT TO UNLIMITED LIABILITY AND THEREFORE COULD NOT UNDERWRITE THIS EXPOSURE. THIS IS FALSE. CONGRESS EXPLICITLY LIMITED A GUARANTOR'S LIABILITY TO THE AMOUNT OF THE FINANCIAL RESPONSIBILITY PROVIDED AND NO MORE. FOR THE PAST 24 YEARS IN WHICH FINANCIAL RESPONSIBILITY HAS BEEN PROVIDED BY GUARANTORS, WE KNOW OF NO INSTANCE IN WHICH THE GUARANTOR'S LIMITS HAVE BEEN BREACHED. CONGRESS BUILT A CASTLE IN THE FORM OF SECTION 1016(G) OF OPA 90 ENSURING THIS LIMIT. THE COAST GUARD NOW HAS BUILT A MOAT AND A BARBED WIRE FENCE AROUND THE CASTLE. WE BELIEVE AMENDMENTS MADE TO THE GUARANTY FORMS WILL

REINFORCE OPA 90'S CLEAR LIMITATION ON A GUARANTOR'S LIABILITY AND INCREASE A GUARANTOR'S COMFORT ZONE. WE HAVE INCLUDED SPECIFIC DEFENSES REINFORCING OPA 90'S PROTECTIONS FOR GUARANTORS. WE HAVE NOT, OF COURSE, ADOPTED THE BROAD RANGE OF POLICY DEFENSES NORMALLY AVAILABLE TO INSURERS IN THEIR UNDERLYING INSURANCE CONTRACTS. AS WE HAVE CONSISTENTLY STATED, ALLOWING THE FULL RANGE OF POLICY DEFENSES WOULD MAKE OPA 90'S "POLLUTER PAYS" PRECEPT RATHER HOLLOW AND WOULD PROVIDE CLAIMANTS WITH NO ASSURANCE OF PAYMENT BY A GUARANTOR. COMPANIES SUCH AS WQIS, SHORELINE, AND FIRST LINE HAVE NOT OBJECTED TO THE NON-INCLUSION OF THESE BROAD POLICY DEFENSES.

THE LAST MAJOR ASPECT OF THE RULE I'D LIKE TO MENTION IS THE IMPLEMENTATION SCHEDULE. ALTHOUGH THE REGULATORY TEXT MAY APPEAR COMPLICATED, THE CONCEPT IS SIMPLE. SELF-PROPELLED TANK VESSELS ARE THE FIRST GROUP OF VESSELS FOR WHICH NEW FINANCIAL RESPONSIBILITY MUST BE DEMONSTRATED -- BY DECEMBER 28, 1994. TANK BARGES ARE THE SECOND GROUP, BY JULY 1, 1995. FINALLY, ALL OTHER VESSELS (PASSENGER VESSELS, DRY CARGO VESSELS, ETC.) MUST COMPLY, ON A STAGGERED THREE-YEAR BASIS, AS THEIR PREEXISTING COFRS EXPIRE, BEGINNING DECEMBER 28, 1994. THE RULE WAS MADE EFFECTIVE UPON PUBLICATION TO PREVENT VESSEL OPERATORS IN THIS LATTER CATEGORY FROM RENEWING A COFR EARLY IN ORDER TO EXTEND THE COMPLIANCE DATE. HOWEVER, NO VESSEL OPERATOR IS REQUIRED TO DEMONSTRATE FINANCIAL RESPONSIBILITY UNDER THE NEW RULE BEFORE DECEMBER 28, 1994.

IT HAS BEEN ASSERTED THAT THE COAST GUARD, IN ADOPTING THIS RULE, IS IMPOSING UNREASONABLE AND EXCESSIVE COSTS ON INDUSTRY.

THE COAST GUARD DOES NOT BELIEVE THE COSTS ARE EXCESSIVE, AND MORE IMPORTANTLY, THE COAST GUARD IS NOT IMPOSING THESE COSTS. SHIPOWNERS, AFTER LENGTHY INTERNAL DEBATE, HAVE THUS FAR CHOSEN TO IMPOSE THESE COSTS UPON THEMSELVES. THE P&I CLUBS ARE THE SHIPOWNERS, AND THE MAJOR SHIPOWNERS ACT AS THE BOARDS OF THE CLUBS AND VOTE THE DECISIONS FOR THE CLUBS. SHIPOWNERS CONFIRMED TO THE COAST GUARD RULEMAKING DOCKET THAT, THUS FAR, THEY SUPPORT THE DECISIONS TAKEN BY THEIR BOARDS THAT THE CLUBS SHOULD NOT PROVIDE THE INSURANCE GUARANTIES TO THE COAST GUARD. CLEARLY, IF THESE SHIPOWNERS DO NOT WISH TO INCUR THE ADDITIONAL COSTS OF PURCHASING FINANCIAL RESPONSIBILITY GUARANTIES FROM COMMERCIAL SOURCES, THEY CAN DIRECT THEIR CLUBS TO ISSUE THE GUARANTIES, PRESUMABLY AT LESS COST THAN FROM THE ALTERNATIVE COMMERCIAL SOURCES.

WHAT MIGHT THESE COSTS BE? IF THE CLUBS DO NOT PROVIDE THE GUARANTIES -- AND THAT IS THE ASSUMPTION UPON WHICH OUR DECISIONS HAVE BEEN BASED -- WE EXPECT A NUMBER OF ALTERNATIVE POSSIBILITIES TO EMERGE. WITH RESPECT TO THE OCEAN-GOING FLEET, TWO NEW INSURANCE COMPANIES ARE EMERGING-- SHORELINE, AN INDEPENDENT MUTUAL CLUB, AND FIRST LINE, AN INSURANCE COMPANY. NEITHER OF THESE COMPANIES HAS YET BEEN DEEMED ACCEPTABLE BY THE COAST GUARD, BUT WE EXPECT THEY BOTH WILL BE SEEKING APPROVAL VERY SOON. THERE MAY BE OTHER INSURANCE COMPANIES DEVELOPING PLANS TO OFFER INSURANCE GUARANTIES FOR THE OCEAN-GOING FLEET. SURETY UNDERWRITERS ARE EXPECTED TO OFFER SURETY BOND GUARANTIES. THE DOCKET CONTAINS COMMENTS FROM ONE SURETY BROKER REPRESENTING UNDERWRITERS WITH A COMBINED TREASURY-APPROVED UNDERWRITING

CAPACITY EXCEEDING $1 BILLION, WELL IN EXCESS OF THE LARGEST AMOUNT OF FINANCIAL RESPONSIBILITY REQUIRED. WE RECENTLY WERE MADE AWARE OF ANOTHER WELL-KNOWN BROKERING COMPANY MARKETING SURETY BONDS AS WELL, AND THERE ARE LIKELY TO BE OTHERS.

ANOTHER AVENUE FOR DEMONSTRATING FINANCIAL RESPONSIBILITY IS SELF-INSURANCE. THE SELF-INSURANCE CRITERIA ARE THE SAME AS PROPOSED AND AS HAVE EXISTED SINCE THE BEGINNING OF THIS PROGRAM. TANGIBLE U.S. ASSETS ARE REQUIRED -- ASSETS LOCATED AWAY FROM THE JURISDICTION OF THE UNITED STATES' COURTS CANNOT BE USED IN THE NET WORTH AND WORKING CAPITAL CALCULATIONS. WE HAVE HEARD THAT COMPANIES ARE SERIOUSLY CONSIDERING THIS METHOD, AND THE AMERICAN PETROLEUM INSTITUTE REPORTED TO SECRETARY PEÑA THAT MAJOR OIL COMPANIES COULD ADOPT ACCEPTABLE SELF-INSURANCE ARRANGEMENTS. THIS SELF-INSURANCE COULD BE USED TO PROVIDE FINANCIAL RESPONSIBILITY FOR BOTH OWNED VESSELS AND BAREBOAT CHARTERED VESSELS WITHIN A COMPANY'S FLEET.

SO, IF THE P&I CLUBS DO NOT PROVIDE GUARANTIES, WE EXPECT A MIX OF ALTERNATIVE OPPORTUNITIES. THE COAST GUARD HAS NOT BASED ITS DECISION ON THE EXPECTATION THEY WILL ALL MATURE. MARKET-BASED FACTORS WILL DICTATE WHICH OF THESE WILL BE USED.

IT IS DIFFICULT TO PREDICT THE COST OF COMMERCIAL GUARANTIES. UNTIL THE RULE WAS PROMULGATED, POTENTIAL GUARANTORS WERE UNABLE TO FIRM UP PREMIUM REQUIREMENTS. NEVERTHELESS, THE COAST GUARD IN ITS REGULATORY IMPACT ANALYSIS (RIA), STRICTLY FOR HYPOTHETICAL ANALYSIS, USED A WORST-CASE COST SCENARIO, IN WHICH THE COST OF GUARANTIES WAS SEVEN TIMES THE COST OF THE P&I CLUBS' OPA 90 SURCHARGE. WE BELIEVE THIS ESTIMATE WILL FAR EXCEED THE

ACTUAL COST. EVEN THIS GROSS OVERESTIMATION TRANSLATES TO LESS THAN TWO-FIFTHS OF ONE CENT PER GALLON OF GASOLINE AT THE PUMP. IT IS EXPECTED THAT THESE POLLUTION INSURANCE COSTS WILL BE A COMPONENT OF WORLDSCALE AND PASSED ON DOWN THE CONSUMPTION CHAIN.

A RECENT ARTICLE REPORTING ON THE PROPOSED COSTS OF SHORELINE'S INSURANCE GUARANTIES CONFIRMS OUR ASSUMPTIONS. SHORELINE'S REPORTED COSTS, FROM 19 CENTS PER DEADWEIGHT TON FOR SOME TANKERS TO 76 CENTS FOR OLDER TANKERS, IS WELL BELOW THE WORST-CASE ESTIMATE IN OUR RIA. THE PREMIUMS FOR NON-TANK VESSELS ARE EXPECTED TO BE FAR LESS. WE HAVE HEARD REPORTS THAT SURETY BONDS WILL COST ABOUT ONE-HALF OF ONE PERCENT TO ONE PERCENT OF THE BOND AMOUNT. THE ONLY COST OF SELF-INSURANCE AND FINANCIAL GUARANTIES IS THE COST OF MAINTAINING INDEPENDENTLY AUDITED FINANCIAL STATEMENTS. SO, ALTHOUGH THERE MAY BE COSTS, THESE COSTS ARE NOT CONSIDERED EXCESSIVE, AND ARE COSTS THE SHIPOWNERS THEMSELVES HAVE DECIDED TO INCUR.

AS TO POSSIBLE COSTS TO THE INLAND AND SMALL-VESSEL COASTAL FLEET, I NOTED BEFORE THAT THIS "BROWN-WATER" FLEET HAS BEEN WELL-SERVED BY WQIS. WQIS CURRENTLY PROVIDES THIS FLEET WITH STRAIGHT LIABILITY INSURANCE (THAT IS, NOT INDEMNITY COVERAGE) INCLUDING LIABILITY FOR OPA 90 COSTS AND DAMAGES AT OPA 90'S LIMITS OF LIABILITY. WE EXPECT WQIS TO BE ABLE TO CONTINUE TO PROVIDE THE INSURANCE GUARANTIES UNDER THE NEW RULE. IF WQIS HAS TO RAISE PREMIUMS BECAUSE OF OPA 90, ALL OF THIS FLEET'S OPERATORS LIKELY WILL BE AFFECTED AND THERE WILL BE A LEVEL PLAYING FIELD.

OUR RULE DOES NOT ADOPT THE PROPOSED MANDATORY EXCESS INSURANCE FACILITY (MEIF). THE MEIF WAS CONCEIVED BY A GROUP OF

INTERNATIONAL SHIPOWNERS CONCERNED ABOUT THEIR EXPOSURE TO POTENTIAL UNLIMITED LIABILITY. MOST OF THESE SHIPOWNERS ROUTINELY CARRY $700 MILLION OF OIL POLLUTION INSURANCE, AND SOME OBTAIN MORE, PERHAPS FOR A TOTAL OF $1 BILLION. GIVEN THE MEASURE OF COSTS AND DAMAGES IN THE EXXON VALDEZ CASE, THESE SHIPOWNERS FEAR THEY ARE OPERATING UNDERINSURED. ACCORDINGLY, THEY PROPOSED THE CREATION OF THE MEIF AS A MEANS OF OBTAINING HIGHER LEVELS OF INSURANCE -- AT LEAST ANOTHER BILLION OR TWO -- NOT GENERALLY AVAILABLE IN THE COMMERCIAL MARKETPLACE. SECONDARILY, THE MEIF MIGHT SERVE AS A COFR GUARANTOR IN COMPETITION WITH COMMERCIAL GUARANTIES. THE MEIF REQUIRES LEGISLATION. THERE ARE MANY UNANSWERED QUESTIONS; THIS IS NECESSARILY A LONG-TERM EFFORT. HENCE, THE COAST GUARD REJECTED THE MEIF AS A SOLUTION TO THE PRESENT COFR MATTER, ESPECIALLY SINCE OTHER COMMERCIAL ALTERNATIVES WOULD BE MADE AVAILABLE AND THIS RULEMAKING STARTED IN 1991. NEVERTHELESS, THE COAST GUARD BELIEVES THAT THE CONCERNS OF THE MEIF PROPONENTS SHOULD BE STUDIED FURTHER, AND THE COAST GUARD HAS COMMITTED ITSELF TO CONTINUE EXAMINING THIS PROPOSAL.

MR. CHAIRMAN, THE ADMINISTRATION HAS DELIBERATED A LONG TIME BECAUSE WE WANTED TO BE SURE WE WERE DOING THE RIGHT THING, AND NOT UNREASONABLY PREJUDICING INDUSTRY. WE ALSO WANTED TO ASSURE OURSELVES THAT WE DID NOT STRAY FROM CONGRESS' MANDATE IN OPA 90. AS TIME PASSES, WE ARE MORE CONFIDENT THAN EVER THAT WE HAVE MADE THE RIGHT DECISIONS, AND OUR FAITH IN THE COMMERCIAL MARKET PLACE HAS BEEN REINFORCED. IN THE TIME SINCE PUBLICATION EARLY THIS MONTH, WE HAVE BEEN ENCOURAGED BY THE RESPONSE TO OUR RULE. WE

HAVE TALKED WITH AND BRIEFED NUMEROUS INDIVIDUALS AND GROUPS, INCLUDING THE STAFFS OF THE RELEVANT CONGRESSIONAL COMMITTEES. WE HAVE AN OPEN DOOR. THE DEPARTMENT OF TRANSPORTATION IS COMMITTED TO ENSURING THE PUBLIC UNDERSTANDS THE RULE. WE DON'T WANT THE PUBLIC OPERATING ON RUMOR AS IT HAS SINCE 1991. I AM PROUD OF THIS RULE. IT HAS BEEN ONE OF THE COAST GUARD'S MOST WIDELY DEBATED AND EXAMINED RULES. I NOW LOOK FORWARD TO ITS IMPLEMENTATION.

THANK YOU FOR THE OPPORTUNITY TO SHARE THIS INFORMATION WITH YOU. I WILL BE HAPPY TO RESPOND TO ANY QUESTIONS THAT YOU OR OTHER MEMBERS OF THE COMMITTEE MAY HAVE.

U.S. Department of Transportation
United States Coast Guard

National Pollution Funds Center

FOR IMMEDIATE RELEASE
Thursday, June 30, 1994

NPFC 94-04
Contact: External Affairs
Tel.: (703)235-4709

COAST GUARD COMMANDANT ANNOUNCES
VESSEL FINANCIAL RESPONSIBILITY RULE

Admiral Robert E. Kramek, the Commandant of the U.S. Coast Guard, announced the issuance of the long-awaited Certificate of Financial Responsibility (COFR) rule, which specifies what types of evidence vessel owners and operators must submit to the Coast Guard to demonstrate the ability to pay damages and removal costs in the event of oil or hazardous substance spills. The COFR rule implements portions of the Oil Pollution Act of 1990 (OPA 90) and the Comprehensive Environmental Response, Compensation and Liability Act (Superfund), both of which require vessel owners and operators to present "evidence of financial responsibility" of their ability to pay up to the limits specified in each law. OPA 90, which concerns discharges of oil, was enacted partly in response to the *EXXON VALDEZ* incident. Superfund deals with releases of hazardous substances other than oil. This rule was approved by the Secretary of Transportation and the Office of Management and Budget.

The administrative process of developing the COFR rule has been carefully watched and commented on by international shipping interests, who have voiced concern over the financial responsibility and liability aspects of OPA 90. The new financial responsibility requirements draw heavily from the original September 1991 rulemaking proposal, but the Coast Guard has made a number of technical and implementation schedule changes in response to industry comments. Shipowners and operators will be allowed to demonstrate financial responsibility through types of self-insurance that require tangible assets, as well as insurance guaranties and surety bond guaranties. However, the Coast Guard has not adopted various maritime industry proposals to allow the use of membership in shipowner associations (known as P&I Clubs) as self-insurance without tangible assets.

Several shipowners' organizations proposed the creation of a Mandatory Excess Insurance Facility (MEIF), which would provide high levels of liability coverage as well as serve as a guarantor for the purpose of providing COFR coverage. This proposal was not accepted by the Coast Guard because it would require substantial legislation. However, even though it involves primarily non-COFR-related issues, Admiral Kramek has recommended

that the concept be further considered as a means of addressing shipowners' concerns about their inability to purchase multi-billion dollar levels of oil pollution liability coverage in the commercial market. That amount of insurance far exceeds any COFR-related financial responsibility requirements.

Insurers and other providers of financial responsibility (called guarantors) will be subject to direct action from claimants, as provided in OPA 90. However, the rule restates and reinforces OPA 90's provision that a guarantor's liability under direct action is strictly limited to the amount of the guaranty provided. A guarantor is, by law, not subject to unlimited liability.

The Coast Guard also prepared a final Regulatory Impact Analysis (RIA). The RIA concludes that the rule will not cause severe economic disruption (a "train-wreck"). Even if shipowners continue to prohibit their P&I Clubs from providing the OPA 90 financial responsibility guaranties, commercial sources say they will make the guaranties available.

Although the rule is effective upon publication, the Coast Guard is allowing 90 days for comments, particularly on the changes made from the September 1991 proposal. After reviewing all comments and making necessary changes, the Coast Guard will publish a final rule.

An implementation schedule that allows a non-disruptive transition to compliance with the new rule has been provided. Self-propelled tank vessels generally will be the first category of vessels required to comply with the new rule, by December 28, 1994. Tank barges must be in compliance by July 1, 1995. Non-tank vessels must comply when their existing COFRs expire, beginning December 28, 1994.

Further questions concerning vessel financial responsibility may be directed to the Coast Guard's National Pollution Funds Center at (703)235-4709.

NPFC

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U.S. Department of Transportation
United States Coast Guard

National Pollution Funds Center

June 30, 1994

VESSEL CERTIFICATES OF FINANCIAL RESPONSIBILITY (COFRS)
INTERIM RULE FACT SHEET

1. PURPOSE

The purpose of this fact sheet is to elaborate on the COFR rule to be published in the Federal Register on 1 July 1994.

2. RULE HISTORY

Oil Pollution Act of 1990 (OPA 90) enacted 18 August 1990
COFR NPRM published 26 September 1991
Extended comment period closed 24 January 1992
Preliminary Regulatory Impact Analysis announced 21 July 1993
Comment period on PRIA closed 20 September 1993
Interim Rule published 1 July 1994
Comment period closes 29 September 1994
Final RIA announced 1 July 1994

3. WHAT DOES THE RULE REQUIRE?

The rule requires a vessel operator basically to do the same thing it has been doing since 1970-- submit to the Coast Guard evidence that it is capable of paying for costs of an oil or hazardous substance spill emanating from its vessel. This is ordinarily done by submitting to the Coast Guard an insurance guaranty form, but some operators prefer a surety bond guaranty form or self-insurance. If an oil or a hazardous substance spill occurs, and the responsible party does not pay, then the insurer or other financial responsibility provider (known as a guarantor) will have to pay costs and damages up to the limits specified in its guaranty.

4. WHAT IS THE RULE DESIGNED TO ACHIEVE?

The rule is designed to implement Congress' intent that a responsible party (rather than U.S. consumers and taxpayers) pays promptly and with assurance for removal costs and damages resulting from an oil or a hazardous substance spill.

5. ARE OPA 90'S FINANCIAL RESPONSIBILITY REQUIREMENTS DIFFERENT FROM PREVIOUS LAWS?

The financial responsibility mechanics are essentially the same as they have been since 1970. OPA 90 increased the limits of

liability for an accidental spill and made it more likely that a responsible party would pay for total costs and damages resulting from an oil spill caused by the responsible party's fault. However, OPA 90 does not expose the guarantor to this unlimited liability. OPA 90 also broadens the types of damages for which a responsible party and its guarantor may be liable. Among these are natural resources damages. Similar to pollution laws in other countries around the world, OPA 90 (like the Outer Continental Shelf Lands Act and the Trans-Alaska Pipeline Authorization Act) allows any person suffering damage to be a claimant directly against the responsible party or guarantor.

6. DOES OPA 90 PREEMPT STATE LAWS?

Just like all pre-OPA 90 pollution laws, OPA 90 leaves intact all state oil spill liability and compensation laws. Moreover, OPA 90 provides that in an action under state (or Federal) law, shipowners may not avail themselves of the protections afforded by the Limitation of Liability Act. That Act allows a shipowner to limit liability to the value of the vessel, plus any earned freight money, often a very small, and sometimes non-existent, amount.

7. WHEN MUST VESSEL OWNERS AND OPERATORS COMPLY WITH THE NEW RULE?

The compliance for a vessel depends on its type: self-propelled tank vessel; non-self-propelled tank vessel; and all other vessels.

Self-propelled Tank Vessels: Tank vessels must demonstrate financial responsibility under the new rule by 28 December 1994. This means that either a new insurance guaranty form or other acceptable evidence of financial responsibility must be filed with the NPFC by this date. Assuming acceptable evidence of financial responsibility is filed by this date, the preexisting COFR may continue to be carried aboard a vessel until 28 December 1995, by which time a new application must have been filed and a new COFR obtained and placed aboard the vessel.

Non-self-propelled Tank Vessels (barges): Barges must file new applications and new financial responsibility guaranties, and obtain new COFRs by 1 July 1995.

All Other Vessels: All other vessels are required to file new applications and evidence of financial responsibility, and obtain new COFRs, before the preexisting COFR for that vessel operator expires. Thus, some vessel operators may be required to obtain new COFRs as early as 28 December 1994 and others as late as 28 December 1997.

8. WHAT TYPES OF FINANCIAL RESPONSIBILITY WILL BE ACCEPTED?

Financial responsibility may be in the form of an insurance guaranty, a surety bond guaranty, a financial guaranty, self-

insurance, or by obtaining NPFC approval of some other evidence that meets the requirements of the new rule. Other evidence could be a specialized letter of credit, for example. Any provider of "other evidence" is considered a guarantor.

Except for the "other evidence" method, the other methods are essentially as proposed in the NPRM.

9. WHAT CHANGES WERE MADE TO THE NPRM?

There were several improvements of a technical nature suggested by commenters and these have been incorporated into the new rule. Some of the more significant changes are: the guaranty forms have been amended to state clearly the defenses that will be allowed guarantors (the defenses are designed to reinforce OPA 90's explicit provision that a guarantor cannot be held liable for more than the amount of financial responsibility provided); a defense that the guaranty provided to the Coast Guard does not serve as a guaranty under state law, without the guarantor's permission, has been created; and a co-subscribing guarantor may choose to subscribe to a limited participation in a guaranty, altering the guarantors' joint and several liability in preexisting financial responsibility undertakings.

10. WHY DID IT TAKE FOUR YEARS TO ADOPT THIS RULE?

The international vessel owning and operating community, directly and through their P&I Clubs, and Lloyd's of London, an insurer and principal reinsurer of the P&I Clubs, strenuously objected to OPA 90's inclusion of potential unlimited liability for those who, through their own fault, caused oil spills in U.S. waters. The Clubs, at the direction of their vessel owner members, stated they would not to issue the financial responsibility guaranties required by OPA 90, despite their issuing similar guaranties to other governments pursuant to the 1969 Civil Liability Convention, and to the United States under various pre-OPA 90 laws. This refusal raised the spectre that these very same vessel owners and operators would not obtain guaranties, and would thereby be precluded from lawfully trading to the United States. This threatened "train wreck" caused the Coast Guard and two Administrations to proceed cautiously, looking at every possible option, while at the same time endeavoring to preserve Congress' intent that the polluter pay for removal costs and damages. The Preliminary Regulatory Impact Analysis the Coast Guard issued last summer elicited a number of important comments that supported the Coast Guard's belief that a train wreck simply would not occur if the proposed rule was adopted. The comments to the docket revealed that alternative (commercial) sources of financial responsibility guaranties would be available if the international vessel owning and operating community persisted in refusing to issue its own guaranties through their P&I Clubs. Having satisfied itself that commercial alternatives would be available, and that the proposed approach best fulfills Congressional intent, the Coast Guard proceeded with development of this rule.

11. WHO IS A GUARANTOR?

A guarantor is any entity that provides evidence of financial responsibility on behalf of a responsible party. Examples are an insurance company that executes the insurance guaranty form appended to the interim COFR rule, or a surety company that executes the surety bond guaranty form appended to the interim rule.

12. ARE GUARANTORS SUBJECT TO UNLIMITED LIABILITY?

No. Section 1016(g) of OPA 90, as did previous pollution laws, explicitly states that a guarantor's liability is limited to the amount of the financial responsibility provided a responsible party. The COFR rule restates this principle, and, in addition, the guaranty forms appended to the rule make this limitation a defense.

13. WHO IS SUBJECT TO DIRECT ACTION?

A person (such as an insurer or surety company) that agrees to act as a guarantor is subject to direct action. A responsible party is also subject to suit to recover costs and damages from an oil spill or hazardous substance release.

14. CAN A P&I CLUB OR OTHER ENTITY PROVIDE EVIDENCE OF FINANCIAL RESPONSIBILITY AND NOT BE A GUARANTOR?

No, if the Club or other entity executes the insurance or other guaranty form. On the other hand, an entity acting as a reinsurer of another entity that executes the insurance or other guaranty form would not be a guarantor. No one becomes a financial responsibility provider (guarantor) under the interim rule without executing a guaranty form. Therefore, there can be no "cut-through" to a reinsurer solely because of the guaranty provided by the direct insurer.

15. WHERE CAN OWNERS AND OPERATORS OBTAIN GUARANTIES?

Guaranties may be obtained from insurers, sureties and other persons deemed acceptable by the Coast Guard. Established marine insurance brokers are aware of the identities of these companies. Many of these companies provided comments to the official Coast Guard docket.

16. WHAT ARE THE NAMES OF ACCEPTABLE INSURANCE COMPANIES OTHER THAN THE P&I CLUBS?

There are a number of insurance companies acceptable for purposes of providing guaranties under the preexisting financial responsibility rules. The Coast Guard does not know specifically which of these companies will offer OPA 90/CERCLA guaranties. Up to now the major guarantors have been the Water Quality Insurance Syndicate in New York City and the international P&I Clubs. The

comments to the regulatory docket contain letters from at least two new commercial entities, Shoreline Mutual and First Line, that may offer insurance guaranties. There are also letters from surety companies indicating a willingness to provide surety bond guaranties.

17. HAVE SHORELINE AND FIRST LINE BEEN APPROVED BY THE COAST GUARD?

No. Neither of these companies has submitted a formal request to the Coast Guard in order to be found acceptable. However, based on the comments to the regulatory docket, we expect that these, and possibly other companies, will seek Coast Guard determinations of acceptability soon.

18. WHAT WILL BE THE COST OF GUARANTIES FROM NEW COMPANIES SUCH AS SHORELINE OR FIRST LINE?

The Coast Guard is not yet privy to the actual premiums or "calls" these companies will charge owners and operators. The cost of these guaranties for non-tank vessels will, of course, be less than for tank vessels. For tank vessels, the Regulatory Impact Analysis concludes that the premiums are expected to result in costs to the ultimate consumer of a gallon of refined product of, at most, two-fifths of one cent.

19. WHAT CAN AN OWNER OR OPERATOR DO IF IT CANNOT OBTAIN AN INSURANCE GUARANTY OR A SURETY BOND GUARANTY?

If that the owner/operator is unable to self-insure or obtain a financial guaranty from a parent or affiliated company, or some other company, the vessel may not operate in U.S. waters. However, we expect that an owner or operator of a good quality vessel will be able to obtain either an insurance or surety bond guaranty.

20. WHY WON'T THE P&I CLUBS ISSUE THE GUARANTIES?

The Clubs have expressed reasons why they won't provide the guaranties, none of which are convincing to the Coast Guard. The Coast Guard does not understand, for example, why the Club members would prefer to pay additional premiums to obtain insurance guaranties from commercial insurers rather than having their own Clubs provide these guaranties, presumably at far less cost. Whatever the reason, this is a business decision in the hands of the shipowners themselves.

21. WHY WON'T THE COAST GUARD ALLOW MEMBERSHIP IN A P&I CLUB, MAKING THE OIL SPILL LIABILITY TRUST FUND A LOSS-PAYEE, TO BE CONSIDERED SELF-INSURANCE?

A P&I Club policy is indemnity insurance, not self-insurance. Neither Generally Accepted Accounting Principles (GAAP) nor any other accounting rules permit the face value of an insurance

policy to be counted as an asset in a net worth determination. This is because there can be no self-insurance without assets set aside to meet potential liabilities. P&I Club insurance requires the vessel owner to pay claims out of the owner's own pocket first, before requiring a Club to reimburse the owner. Moreover, this concept would discriminate against other insurance companies who agree to pay claimants directly. Most importantly, it provides no assurance of payment. A Club could invoke policy defenses, leaving claimants and the vessel owner with nothing. The assignment also requires the assent of the P&I Clubs, and the International Group of P&I Clubs commented to the record that the Clubs had neither approved nor disapproved of this concept. One Club stated it would not give its consent.

22. WHY CAN'T P&I CLUB MEMBERSHIP BE CONSIDERED "OTHER EVIDENCE" OF FINANCIAL RESPONSIBILITY?

The Coast Guard has provided an "other evidence" category in the interim rule. However, by OPA 90's terms, a provider of other evidence of financial responsibility would be a guarantor, and it is this guarantor status to which the P&I Clubs object. Thus, the "other evidence" method does not solve the Clubs' concerns. OPA 90 is different than some state laws which have been cited as precedent for allowing the "other evidence" method. In addition, states have the luxury of knowing that the Oil Spill Liability Trust Fund (OSLTF) is available as a funding source of last resort. There is no similar protection to the OSLTF.

23. WHY WAS THE MANDATORY EXCESS INSURANCE FACILITY (MEIF) REJECTED?

The MEIF cannot be considered a prompt solution to the issue in the COFR rulemaking because legislative action would be required. Also, the Coast Guard felt, and the MEIF promoters agreed, that the MEIF is principally designed to alleviate shipowners' concerns about unlimited liability, not COFRs, which have no relation to one another. Because the MEIF requires legislation, the MEIF concept has not been fully developed from the funding, government oversight, possible tax code, or budgetary standpoints. Thus, the Coast Guard concluded that the MEIF could not be adopted in the context of the COFR rule, but that it should be considered further as a follow-on item. Accordingly, the Coast Guard announced in the preamble to the rule that it would consider further the MEIF for the purpose of addressing shipowners' concerns about operating underinsured in an unlimited liability environment.

24. WHO SUPPORTS THIS RULE?

The rule has been supported by environmental organizations, the state of Alaska, and by companies interested in providing financial responsibility guaranties in place of the P&I Clubs.

25. WHO OPPOSES THIS RULE?

The NPRM, and presumably this rule, has been opposed by the international shipping industry, led by tanker owners. Lloyd's of London also has opposed the rule. All opponents would greatly prefer the United States to adopt the more lenient international liability law in place of OPA 90. The U.S. Congress, however, has been equally adamant that the United States will retain essential characteristics of OPA 90 that are incompatible with the international system, namely, potential unlimited liability for responsible parties and non-preemption of state liability laws.

26. WHERE CAN OPERATORS DIRECT THEIR QUESTIONS ABOUT COMPLYING WITH THE NEW RULE?

Persons having questions about how to comply with the new rule should contact the Coast Guard National Pollution Funds Center's Vessel Certification division at (703) 235-4810, telefax (703) 235-4835.

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COMPLIANCE SCHEDULE OF NEW COFR RULES FOR SELF PROPELLED TANK VESSELS*

(FEDERAL REGISTER PUBLICATION DATE OF JULY 1, 1994)

*This chart illustrates the COFR rule's implementation plan. If there is a conflict between this chart and the rule, the rule controls.

	7/1/94 through 12/27/94	12/28/94 through 12/27/95	Before 12/28/95	12/28/95
Vessel has old COFR prior to 7/1/94.	Vessel may continue to operate with old COFR.	Vessel must demonstrate new financial responsibility by 12/28/94. If demonstrated, vessel's old COFR is valid until 12/28/95.	Vessel must file a new COFR application form and obtain a new COFR.	Vessel must carry new COFR.
Vessel has old COFR that expires after 6/30/94 but before 12/28/94.	Vessel must renew old COFR before expiration date to continue operations in U.S. waters.	Vessel must demonstrate new financial responsibility by 12/28/94. If demonstrated, vessel's old COFR is valid until 12/28/95.	Vessel must file a new COFR application form and obtain a new COFR.	Vessel must carry new COFR.
Vessel has old COFR, but does not demonstrate new financial responsibility requirements by 12/28/94.	Vessel may continue to operate with old COFR.	Vessel's old COFR is revoked, and must file new COFR application form and demonstrate new financial responsibility.		
Vessel's old COFR expires after 12/27/94 but before 12/28/95.	Vessel may continue to operate with old COFR.	Vessel must demonstrate new financial responsibility by 12/28/94, and old COFR is deemed extended until 12/28/95.	Vessel must file a new COFR application form and obtain a new COFR.	Vessel must carry new COFR.

COMPLIANCE SCHEDULE OF NEW COFR RULES FOR NON-SELF PROPELLED TANK VESSELS*

(FEDERAL REGISTER PUBLICATION DATE OF JULY 1, 1994)

*This chart illustrates the COFR rule's implementation plan. If there is a conflict between this chart and the rule, the rule controls.

	7/1/94 through 6/30/95	Before 7/1/95	7/1/95
Vessel has an old COFR prior to 7/1/94 that does not expire until after 6/30/95.	Vessel may continue to operate with old COFR.	Vessel must file a new COFR application form, demonstrate new financial responsibility, and obtain a new COFR by this date.	Vessel must carry new COFR.
Vessel has an old COFR that expires before 7/1/95.	Vessel can renew old COFR before expiration date, or may obtain new COFR in accordance with new rules, after 12/27/94.	Vessel must file a new COFR application form, demonstrate new financial responsibility, and obtain a new COFR by this date.	Vessel must carry new COFR.
Vessel does not have an old COFR but needs a COFR between 7/1/94 and 6/30/95.	Vessel can file old COFR application form and demonstrate old financial requirements to obtain an old COFR or may obtain new COFR in accordance with new rules, after 12/27/94.	Vessel must file a new COFR application form, demonstrate new financial responsibility, and obtain a new COFR by this date.	Vessel must carry new COFR.

COMPLIANCE SCHEDULE OF NEW COFR RULES FOR VESSELS OTHER THAN TANKERS*

(FEDERAL REGISTER PUBLICATION DATE OF JULY 1, 1994)

*This chart illustrates the COFR rule's implementation plan. If there is a conflict between this chart and the rule, the rule controls.

	7/1/94 through 12/27/94	12/28/94 through 12/27/97	12/28/97
Vessel has old COFR prior to 7/1/94 that expires before 12/28/94.	Vessel can file old COFR application form and demonstrate old financial responsibility requirements to obtain an old COFR which is valid for three years.	Prior to the expiration of old COFR, vessel must file a new COFR application form, demonstrate new financial responsibility, and obtain a new COFR.	Vessel must carry new COFR by this date or earlier depending on expiration date of old COFR.
Vessel does not have old COFR but needs a COFR before 12/28/94.	Vessel can file an old COFR application form and demonstrate old financial responsibility requirements to obtain an old COFR which is valid for three years.	Prior to expiration of the old COFR, vessel must file a new application form, demonstrate new financial responsibility, and obtain a new COFR.	Vessel must carry new COFR by this date or earlier depending on expiration date of old COFR.
Vessel surrenders unexpired, old COFR for a name change.	Vessel obtains a replacement of old COFR with same expiration date of the surrendered, old COFR.	Vessel obtains a replacement of old COFR with same expiration date of the surrendered, old COFR. Before replacement COFR expires, vessel must file a new COFR application form, demonstrate new financial responsibility, and obtain a new COFR.	Vessel must carry new COFR by this date or earlier depending on expiration date of old COFR.
Vessel does not have an old COFR but needs a COFR after 12/27/94.	Vessel may apply for new COFR.	Vessel must file a new COFR application form, demonstrate new financial responsibility requirements, and obtain a new COFR, before operating in U.S. waters.	Vessel must carry new COFR by this date.

The Coast Guard concluded in its Regulatory Impact Analysis that the hypothetical worst case cost resulting from the interim rule could be $415 million. The following excerpt from the Regulatory Impact Analysis explains the basis for this cost estimate.

REGULATORY IMPACT ANALYSIS EXCERPT

5. Cost of Commercial Insurance and Surety Bonds

a. Commercial Insurance

As noted earlier, two emerging commercial insurers are likely to provide financial responsibility guaranties to the Coast Guard. First Line's premiums are expected to be based on the type of operation and vessel, as well as the operator's prior record. Oil tankers will be assessed a higher premium than other types of vessels.

Shoreline Mutual's premium would be based upon prior United States oil pollution claims data, rather than on the oil pollution spill record of an individual owner or operator. Discounts would be provided based upon such factors as the age of the ship, whether a vessel is double-hulled, and whether the vessel has any other recognized safety features. Oil tankers would be assessed the highest premiums since they have the greatest risk of causing an oil spill.

For competitive reasons, neither First Line nor Shoreline Mutual provided premium estimates to the Coast Guard. However, to provide some notion of possible costs, this analysis uses as a baseline, the P&I Clubs' OPA 90 surcharge. It is conservatively assumed that premiums assessed by these two companies on all oil tankers that carry oil to the united States would not exceed seven times that surcharge (29 cents per grt per voyage).[98] Using this overly cautious assumption, the additional cost of a barrel of imported crude oil or refined product, such as gasoline, would be less than $0.145. The cost of a gallon of refined product would be $0.00345 (less than two-fifths of a penny).[99] Table Eleven illustrates how much, at most, the added cost of the premiums by these commercial insurers could add at various points along the distribution chain.

These estimates assume that only tankers that carry imported oil to the United States will obtain OPA 90 financial responsibility guaranties from these insurance companies. The P&I Clubs have asserted that they will not provide COFR

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[98]The surcharge is for $500 million of oil pollution cover. First Line intends to provide coverage in amounts needed to obtain COFRs, and Shoreline Mutual's coverage will not exceed $300 million. The factor of seven was selected as an overly cautious estimate of insurance guaranty costs, so as not to under-inflate the possible costs.

[99]The actual impact at the gasoline pump would be less than the $0.00345 estimated for these commercial insurance premiums. Domestic oil supplies account for approximately 54 percent of United States total oil consumption. Most of this will be transported by pipelines or carried by tankers who are not insured by the International Group of P&I Clubs.

guaranties even for dry cargo and passenger vessels. Therefore, these vessels would likely use First Line or Shoreline (or some other insurance entity) in order to meet their OPA 90 financial responsibility requirements. Thus, it is assumed the premiums for non-tank vessels would, to some extent, offset the premiums estimated above for oil tankers. As a result, the cost to the consumer for refined oil products should be less than the estimated $0.00345 a gallon. If commercial insurers are successful in obtaining a premium of $2.03 per grt per voyage, the total cost to the United States consumer for 1994 would be $415 million.[100] It is not known what impact, if any, these commercial insurers' premiums will have on the P&I Clubs' premiums.[101]

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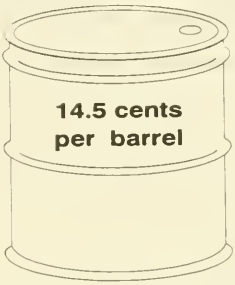
[100]This segment of the analysis assumes that all tankers importing oil are insured by either First Line or Shoreline and no discounts are given. Also it assumes that the United States will import 7.84 million barrels of oil a day via ship for 1994. Oil imports for 1994 requiring water transportation are based upon United States Department of Energy's projections, and a Coast Guard estimate that 1.07 million barrels of oil a day will be supplied by Canada via pipeline for 1994.

[101]It is possible that since First Line and Shoreline Mutual would be absorbing the greatest OPA 90 risks, P&I Club payouts would substantially decrease, thereby possibly reducing the Clubs' reinsurance premium, ultimately offsetting the cost to vessel operators of First Line and Shoreline COFR insurance.

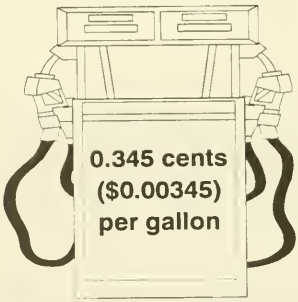
TABLE ELEVEN
ESTIMATED COMMERCIAL INSURANCE COSTS AT VARIOUS POINTS ALONG THE DISTRIBUTION CHAIN

For an oil tanker of 50,000 grt carrying 7000,000 barrels of oil:

For a barrel of imported crude oil at a U.S. refinery:



For a gallon of refined product, such as gasoline:



Note: For competitive reasons, commercial insurers have not provided the Coast Guard with premium estimates. This analysis shows the impact on prices for imported oil throughout the distribution chain if commercial insurers assessed a premium seven times the amount of the P&I Club's oil pollution surcharge, which is 29 cents per grt per voyage for the 1994 policy year. The Coast Guard does not expect commercial insurance to cost that much, but for purposes of this analysis, wishes to provide conservative cost estimates.

AUG 1 1 1994

U.S. Department of Transportation
United States Coast Guard

Commandant
U.S. Coast Guard

2100 Second Street S.W.
Washington, DC 20593-0001
Staff Symbol: G-CC
Phone: (202) 366-4280

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AUG 8 1994

The Honorable W. J. (Billy) Tauzin
Chairman, Subcommittee on Coast Guard
and Navigation
House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

At the Coast Guard and Navigation Subcommittee hearing on July 21, 1994, concerning the Interim Rule for Vessel Certificates of Financial Responsibility, I indicated more information would be provided on options available should shipowners and operators be unable to obtain financial responsibility guaranties as required by our interim rule.

There are various avenues available for demonstrating financial responsibility under the rule, including insurance, surety bonds, financial guaranties, and self-insurance. An "other evidence" method is also available to allow for arrangements that might be developed that do not fit neatly into one of the traditional methods. This rule was not developed with an "all or nothing" scenario contingent on the success of Shoreline or First Line. Rather, the Coast Guard adopted this rule after very careful, lengthy deliberation.

As we indicated at the hearing, the U.S. brown water and coastal fleet still has available its traditional U.S.-based guarantors, such as the WQIS, and the record in this rulemaking documents offers by the substantial and already "acceptable" U.S. surety industry to issue surety bond guaranties to blue water vessels. Further, the U.S. oil majors, and others, can employ methods such as self-insurance and financial guaranties. Additionally, other insurers, including a few non-International Group-affiliated P&I Clubs, such as Ocean Marine, are approved to write OPA 90 guaranties if they choose to do so.

The one tool mentioned at the hearing, suspension of the rule (perhaps more properly described as delay of the compliance date), although legally available, is not an option the Coast Guard envisions invoking. Its mention should not be construed as a signal of intent. Rather, it is a legal avenue that is available to all agencies promulgating rules, but one that is seldom used. We do not anticipate having to use this tool. It would be a disservice to the industry to leave any impression that the Coast Guard is considering a delay of the compliance date. Therefore, industry should conduct its business with the

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Subj: RESPONSE TO THE COAST GUARD AND NAVIGATION SUBCOMMITTEE HEARING ON JULY 21, 1994, CONCERNING THE INTERIM RULE FOR VESSEL CERTIFICATES OF FINANCIAL RESPONSIBILITY (COFRS)

expectation that the rule will not be suspended. It should concentrate its efforts on deciding which options it will use to comply, as we believe industry has the capability to, and will in fact, do so.

As I indicated, we do not believe compliance will be an all or nothing scenario. Many owners and operators already are diligently working towards compliance. In addition to comments in the record, we continue to receive daily very positive indications from a broad segment of the industry that activity continues in the development of ways to facilitate compliance with the rule. It would be unfair to penalize those who make the effort to comply, many of whom are United States companies, by rewarding those who choose not to comply, many of whom are foreign companies. Congress wisely provided the Secretary and President with a mix of enforcement options to deal with those who might elect not to comply. The Oil Pollution Act of 1990 provides various tools for dealing with noncompliance of the regulation. The Ports and Waterways Safety Act provides an additional enforcement tool.

The exercise of any one of the compliance tools necessarily includes the notion of prosecutorial discretion. Each case is examined on its facts, and a decision is made as to whether the action should be prosecuted and, if so, which sanction or sanctions should be applied. At this time, I cannot say which of these tools alone, or in combination, would be utilized to effect our ultimate objective (compliance with the law) while at the same time ensuring that maritime commerce is not significantly disrupted and law-abiding operators are not unduly prejudiced.

I trust this information amplifies the brief remarks we offered at the hearing on this point.

Sincerely,

R. E. Kramek.

ROBERT E. KRAMEK
Admiral, U.S. Coast Guard
Commandant

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 1
COFR HEARING, 21 JULY 94

QUESTION. IN THE INTEREST OF THE SUBCOMMITTEE, I WOULD LIKE TO HAVE THE COAST GUARD PROVIDE ME WITH REGULAR AND TIMELY UPDATES ON THE DEVELOPMENT OF THE VARIOUS ENTITIES THAT WILL PROVIDE THE EVIDENCE OF FINANCIAL RESPONSIBILITY UNDER OPA-90? THIS SHOULD INCLUDE A LIST OF THE ENTITIES AND WHAT STEPS THEY HAVE TAKEN TO MEET THE CRITERIA REQUIRED TO BE APPROVED BY THE COAST GUARD.

Answer. As new information is received, the Coast Guard will advise the Subcommittee about the various entities that are expected to provide evidence of financial responsibility under OPA 90. The following is the current status:

Both Shoreline Mutual's and First Line's representatives have informally told the Coast Guard that they are diligently continuing to finalize their programs. Shoreline has advised that its reinsurance arrangements are nearly complete. Both companies are expected to seek formal acceptance soon.

~~ok~~ The surety industry continues to market surety bond guaranties. The following members from the surety industry have expressed interest in arranging surety bond guaranties:

C.A. Shea & Co., Inc.
Sylvan Corporate Center
910 Sylvan Avenue
Englewood Cliffs, New Jersey 07632
Att: James M. Gorman
Tel: (201)568-2810
Fax: (201)568-0333

International Sureties, Ltd.
837 Gravier Street
Suite 1415
New Orleans, Louisiana 70112-1570
Att: R. Tucker Fitz-Hugh
Tel: (504)581-6404
Fax: (504)581-1876

Underwriters Indemnity
8 Greenway Plaza, Suite 400
Houston, Texas 77046
Att: Edwin H. Frank, III
Tel: (713)961-1300
Fax: (713)961-0285

Willis Corroon Corporation of
North Carolina
301 S. Tryon Street
Two First Union Center
Suite 2600
Charlotte, North Carolina 28282-0001
New York Contact: Charles Steers (212)344-8442
London Contact: Nicholas Taylor (071)488-8111

C.A. Shea and Willis Corroon appear to be the most active in arranging surety bonds. There may be other brokers marketing surety bond guaranties, but they have not identified themselves to the Coast Guard.

A number of companies have informally contacted us concerning self-insurance and financial guaranties. Preliminary conversations indicate that several companies can utilize these methods and intend to do so.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 2
COFR HEARING, 21 JULY 94

QUESTION. WHAT ARE THE SPECIFIC CRITERIA AND STANDARDS REQUIRED FOR COFR INSURERS AND GUARANTORS (INSURANCE ENTITIES, SURETY BOND COMPANIES, AND COMPANIES WHO WISH TO SELF-INSURE) IN ORDER TO MEET FINANCIAL RESPONSIBILITY REQUIREMENTS UNDER OPA-90?

Answer. With respect to insurance companies, we consider each prospective guarantor's approval as an agency adjudication where each case is determined on its own merits, given the totality of the circumstances.

The following criteria are used in our determinations:

a. The first criterion is that prospective guarantors must be financially sound and be able to write risks at the intended level. In the case of stock companies, our general policy with respect to tankships is not to allow retained risks exceeding approximately 5 percent of policyholder surplus or 10 percent of policyholder surplus in the case of non-tankships. In the case of true mutuals, such as the International Group of Protection and Indemnity Clubs, "policyholders surplus" can be a relative term because of the ability of mutuals to call upon their members for additional funds as needed. Therefore, our policy is more flexible concerning the amount of risk on particular undertakings by mutuals.

b. The second criterion is that prospective guarantors must participate in a sound reinsurance program, as implied in the above discussion of the first criterion.

c. Other criteria are willingness to provide financial reports; government oversight at the place domiciled; appointment of a United States agent for service of process; and an unblemished record concerning any previous guaranties filed with the Coast Guard.

An insurer is automatically assumed to meet the first two criteria mentioned above if the insurer has been awarded a "B" or better rating by the well-known professional insurance rating organization, A.M. Best, and has a Best's financial rating commensurate with the size of the net risk the prospective guarantor intends to retain. Our criteria, although perhaps more strict than some agencies, has been consistently applied for many years and is in accord with concepts adhered to by the Maritime Administration, Federal Maritime Commission, and A.M. Best. The Coast Guard recognizes that this is an area where it has some flexibility, and is mindful of Congressional intent to foster a continuing market for OPA 90 guarantors.

With respect to sureties, we rely primarily on determinations made by the U.S. Department of the Treasury, as published in the Federal Register.

With respect to self-insurers and financial guarantors, the specific criteria and standards are published by the Coast Guard at 33 CFR 138.80(b)(3) and (4).

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 3
COFR HEARING, 21 JULY 94

QUESTION. WHAT IS THE ESTIMATED TOTAL COST OF THIS RULE, INCLUDING THOSE COSTS THAT WILL BE BORNE BY VESSEL OWNERS AND OTHERS WHO PARTICIPATE IN THE PROCESS OF SUPPLYING OIL AND OIL PRODUCTS TO THE CONSUMER?

Answer. In its Regulatory Impact Analysis (RIA), the Coast Guard estimated the absolute worst-case COFR costs to oil consumers would be $415 million for 1994 for commercial insurance guaranties, such as from Shoreline Mutual or First Line (see pages 80-82 of the RIA, attached). This translates to less than two-fifths of a penny per gallon of refined product, such as gasoline. This assumed, for purposes of analysis only, that all tank vessels would use the commercial insurance method to meet the COFR requirement, a situation the Coast Guard does not expect to occur. Other methods to meet the COFR rule, such as surety bond guaranties, financial guaranties, and self-insurance, are anticipated to be used, and would result in less costs than the $415 million estimate. A recent Shoreline draft tariff for tank vessel premiums would result in significantly less cost than the Coast Guard's worst-case estimate. Self-insurance and financial guaranties generally cost nothing, and surety bond guaranties increase in attractiveness with the size of an operator's fleet, i.e., the bond premium is the same for a one-vessel fleet as for a one hundred-vessel fleet.

It should also be noted that if the P&I Clubs chose to issue insurance guaranties, shipowners' costs would increase to cover the likely increase in the Clubs' reinsurance premium. The Clubs have never discussed this increased cost. In a recent letter (attached) to Mr. Terrence Coghlin, Chairman of the International Group, the National Pollution Funds Center again requested the Clubs to assist in ascertaining this cost so that the Coast Guard can better assess the true increased cost, if any, attributable to commercial guarantors such as Shoreline or First Line.

5. Cost of Commercial Insurance and Surety Bonds

a. Commercial Insurance

As noted earlier, two emerging commercial insurers are likely to provide financial responsibility guaranties to the Coast Guard. First Line's premiums are expected to be based on the type of operation and vessel, as well as the operator's prior record. Oil tankers will be assessed a higher premium than other types of vessels.

Shoreline Mutual's premium would be based upon prior United States oil pollution claims data, rather than on the oil pollution spill record of an individual owner or operator. Discounts would be provided based upon such factors as the age of

the ship, whether a vessel is double-hulled, and whether the vessel has any other recognized safety features. Oil tankers would be assessed the highest premiums since they have the greatest risk of causing an oil spill.

For competitive reasons, neither First Line nor Shoreline Mutual provided premium estimates to the Coast Guard. However, to provide some notion of possible costs, this analysis uses as a baseline, the P&I Clubs' OPA 90 surcharge. It is conservatively assumed that premiums assessed by these two companies on all oil tankers that carry oil to the United States would not exceed seven times that surcharge (29 cents per grt per voyage).[98] Using this overly cautious assumption, the additional cost of a barrel of imported crude oil or refined product, such as gasoline, would be less than $0.145. The cost of a gallon of refined product would be $0.00345 (less than two-fifths of a penny).[99] Table Eleven illustrates how much, at most, the added cost of the premiums by these commercial insurers could add at various points along the distribution chain.

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[98]The surcharge is for $500 million of oil pollution cover. First Line intends to provide coverage in amounts needed to obtain COFRs, and Shoreline Mutual's coverage will not exceed $300 million. The factor of seven was selected as an overly cautious estimate of insurance guaranty costs, so as not to under-inflate the possible costs.

[99]The actual impact at the gasoline pump would be less than the $0.00345 estimated for these commercial insurance premiums. Domestic oil supplies account for approximately 54 percent of United States total oil consumption. Most of this will be transported by pipelines or carried by tankers who are not insured by the International Group of P&I Clubs.

These estimates assume that only tankers that carry imported oil to the United States will obtain OPA 90 financial responsibility guaranties from these insurance companies. The P&I Clubs have asserted that they will not provide COFR guaranties even for dry cargo and passenger vessels. Therefore, these vessels would likely use First Line or Shoreline (or some other insurance entity) in order to meet their OPA 90 financial responsibility requirements. Thus, it is assumed the premiums for non-tank vessels would, to some extent, offset the premiums estimated above for oil tankers. As a result, the cost to the consumer for refined oil products should be less than the estimated $0.00345 a gallon. If commercial insurers are successful in obtaining a premium of $2.03 per grt per voyage, the total cost to the United States consumer for 1994 would be $415 million.[100] It is not known what impact, if any, these commercial insurers' premiums will have on the P&I Clubs' premiums.[101]

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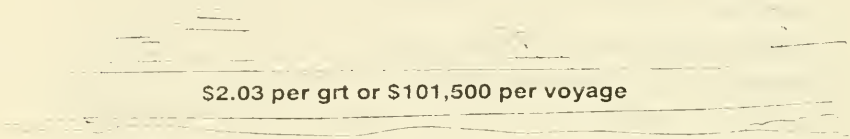
[100]This segment of the analysis assumes that all tankers importing oil are insured by either First Line or Shoreline and no discounts are given. Also it assumes that the United States will import 7.84 million barrels of oil a day via ship for 1994. Oil imports for 1994 requiring water transportation are based upon United States Department of Energy's projections, and a Coast Guard estimate that 1.07 million barrels of oil a day will be supplied by Canada via pipeline for 1994.

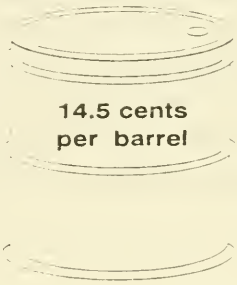
[101]It is possible that since First Line and Shoreline Mutual would be absorbing the greatest OPA 90 risks, P&I Club payouts would substantially decrease, thereby possibly reducing the Clubs' reinsurance premium, ultimately offsetting the cost to vessel operators of First Line and Shoreline COFR insurance.

TABLE ELEVEN
ESTIMATED COMMERCIAL INSURANCE COSTS AT VARIOUS POINTS ALONG THE DISTRIBUTION CHAIN

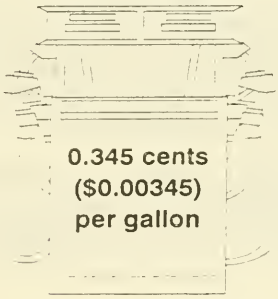
For an oil tanker of 50,000 grt carrying 700,000 barrels of oil:



For a barrel of imported crude oil at a U.S. refinery:



For a gallon of refined product, such as gasoline:



Note: For competitive reasons, commercial insurers have not provided the Coast Guard with premium estimates. This analysis shows the impact on prices for imported oil throughout the distribution chain if commercial insurers assessed a premium seven times the amount of the P&I Club's oil pollution surcharge, which is 29 cents per grt per voyage for the 1994 policy year. The Coast Guard does not expect commercial insurance to cost that much, but for purposes of this analysis, wishes to provide conservative cost estimates.

U.S. Department of Transportation

United States Coast Guard

Director
United States Coast Guard
National Pollution Funds Center

4200 Wilson Boulevard
Suite 1000
Arlington, VA 22203-1804
Staff Symbol: ce
Phone: (703) 235-4704

16450

AUG 22 1994

Mr. Terrence G. Coghlin
Chairman, International Group
of P&I Clubs
c/o Thomas Miller P&I
International House
26 Creechurch Lane
London EC3A 5BA
England

Dear Mr. Coghlin:

It was a pleasure to speak to you again on the occasion of your July 21, 1994, testimony before the Subcommittee on Coast Guard and Navigation, House Committee on Merchant Marine and Fisheries.

Golob's Oil Pollution Bulletin, 29 July 1994, page 5 (copy enclosed) quotes you as testifying that the cost of commercial OPA 90/CERCLA guaranties would be "...greatly in excess of what shipowners are now paying under the P&I Club system for cover which is much broader in scope and higher in amount." The Coast Guard is sensitive to costs imposed by its regulations but, over the years, we have not been able to ascertain the range of per-gross-ton costs to Club members for oil pollution coverage. The Clubs' published, U.S. OPA surcharge is not, of course, the total cost to a shipowner for P&I Club oil pollution cover. In addition to the surcharge there must be added the prorated costs of the advance and other calls. Moreover, as you are aware, the Coast Guard suspects that there may be yet another cost factor that would have to be added. This would be the additional cost resulting from the suspected increased reinsurance treaty premium which would permit the Clubs to issue OPA 90 guaranties comparable to the guaranties proposed to be issued by commercial insurers such as Shoreline Mutual. The latter guaranties, as you pointed out, would cover direct action expenses and some OPA 90 damages which the Clubs are not prepared to cover. Without knowing what these additional Club costs might be, the Coast Guard is comparing apples and oranges.

Accordingly, this is a request for your cooperation in assisting the Coast Guard to provide an oranges to oranges comparison of costs by comparing per-gross-ton costs for commercial OPA 90 guaranties versus hypothetical P&I Club OPA 90 guaranties. Please do not consider this request as an indication that the Coast Guard discounts the Clubs' repeated assurances that they are not prepared to issue OPA 90 guaranties.

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Further, it is expected that the requested cost data will be necessary when responding to questions from the above mentioned subcommittee. If neither the U.K. Club nor the Group wishes to provide such cost data, could you assist the Coast Guard in explaining to the subcommittee how the cost of, for example, Shoreline Mutual's premiums can be said to be greatly in excess of P&I Club system costs?

Thank you, in advance, for your cooperation.

Sincerely,

ROBERT M. SKALL
Technical Coordinator
By direction

Encl: (1) Golob's Oil Pollution Bulletin Article

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 4
COFR HEARING, 21 JULY 94

QUESTION. WHAT OPTIONS DOES THE COAST GUARD HAVE TO ADJUST TO THE COMPLIANCE DATE REQUIREMENTS IF THE RULE DOESN'T "FOSTER A CONTINUING MARKET FOR PROVIDERS OF FINANCIAL RESPONSIBILITY"?

Answer. The Coast Guard does not anticipate adjusting the compliance dates. All indications are that shipowners and operators will have the means to demonstrate evidence of financial responsibility by the compliance dates. Since U.S. surety companies are included in the term, "providers of financial responsibility," the rule already has fostered a continuing market for such providers.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 5
COFR HEARING, 21 JULY 94

QUESTION. HAS THE COAST GUARD ESTABLISHED A DATE WHEN THEY WILL REVIEW THE SITUATION? IS THERE A DATE ESTABLISHED WHEN THE COAST GUARD WILL DECIDE TO MAKE ANY ADJUSTMENTS?

Answer. The Coast Guard assesses the situation on a regular basis, as a result of updated or new information obtained from industry. It is our belief that adjustments other than of a technical nature will be unnecessary, and, therefore, we have not established any date for taking decisions on adjustments.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 6
COFR HEARING, 21 JULY 94

QUESTION. WHAT HAPPENS TO ALL OF THE VESSELS SCHEDULED TO LOAD CARGO AND DEPART IN OCTOBER FOR THE U.S. THAT WILL BE DELIVERED AFTER DECEMBER 28TH AND THEY ARE UNABLE TO FIND AND SECURE EVIDENCE OF FINANCIAL RESPONSIBILITY PRIOR TO LEAVING?

Answer. Congress provided the Coast Guard with a variety of sanctions that can be tailored to meet individual situations. These range from no enforcement to civil penalties to seizure and forfeiture. The Coast Guard will exercise that prosecutorial discretion depending on the facts of each case. However, to reiterate our position, we believe that vessels need not find themselves in the position of non-compliance--there will be ways to comply with the law and regulations. The only change from the present system will be the substitution of commercial guarantors for the P&I Clubs and greater reliance on self-insurance.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 7
COFR HEARING, 21 JULY 94

QUESTION. DURING THE HEARING, MR. SHEEHAN STATED THAT CERTAIN VESSELS WILL NOT BE ABLE TO ATTAIN A COFR UNDER OPA-90 AND WILL NOT BE ALLOWED TO ENTER U.S. WATERS AND HAVE TO TRADE SOMEWHERE ELSE. (SEE TRANSCRIPT PAGES 24-27) WHAT IS THE COAST GUARD'S ANALYSIS ON THE NUMBER OF VESSELS AND ITS PERCENTAGE TO THE WORLD FLEET THAT WILL NOT COMPLY? COULD THIS DISRUPT THE SUPPLY OF OIL TO THE U.S.? WHAT IF THE NUMBERS ARE HIGHER THAN YOUR PREDICTION. HAVE YOU ANALYZED THE HIGHER NUMBERS?

Answer. Mr. Sheehan stated that if some vessels could not comply, those vessels would have to trade elsewhere. He did not predict that vessels would be unable to comply. We believe that they can and will comply. We have no reason to believe that oil shipments to the U.S. will be disrupted. We see no indications that vessel operators who want to trade in our waters will be unable to comply with the law and regulations.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 8
COFR HEARING, 21 JULY 94

QUESTION. UNDER THE METHOD OF "OTHER EVIDENCE", HAS THE COAST GUARD INVESTIGATED ALL POSSIBILITIES OF USING INSURANCE COVERAGE AS AN ASSET IF A VESSEL OWNER WANTS TO SELF-INSURE?

Answer. Yes. We have investigated all the ramifications of this approach, and our reasons for rejecting it are explained in the attached excerpts from the preamble to the interim rule (page 34212) and the Regulatory Impact Analysis (pages 88-97).

C. P&I CLUB MEMBERSHIP AS AN ASSET

1. General Overview

A number of commenters to the NPRM suggested that the Coast Guard should interpret OPA 90 in a manner which would permit it

[106]H.R. Rep. No. 653, 101st Cong., 2d Sess. 120 (1990).

to consider membership in a P&I Club as an asset for the purpose of satisfying the self-insurance option under the proposed regulations. According to the commenters advocating this approach, such an interpretation would enable the P&I Club members to meet the OPA 90 financial responsibility requirements as self-insurers. This also would enable the P&I Clubs to avoid direct action and use their policy defenses, since the P&I Clubs would not be guarantors, i.e., would not be providing any evidence of financial responsibility directly. Accordingly, they claim that this proposal could avoid the need to obtain additional insurance or to purchase surety bonds to obtain COFRs.

A number of state governments accept the membership in a P&I Club approach as a means to meet a state's evidence of financial responsibility requirements. For example, California does not allow vessels lawfully to enter its waters without a California Certificate of Financial Responsibility ("CCFR"). In order to obtain a CCFR, the vessel owner or operator must demonstrate the means to pay at least $500 million for damages resulting from oil pollution. Financial responsibility may be demonstrated in a variety of ways, such as a surety bond, letter of credit, self insurance, proof of insurance, or any combination of the above or any other evidence of financial responsibility. California law, devoid of OPA 90's guaranty requirements, therefore has been interpreted to allow for proof of evidence of membership in a P&I Club as the means to comply with its oil pollution law. The California approach has been followed by Washington and Florida.

Unlike OPA 90, however, these state statutes do not provide for the right of direct action against insurers, which apparently allows these states to adopt this method. Moreover, these states are aware that the OSLTF exists as a backup or alternative source of money in the event their own mechanisms prove ineffective due to policy defenses in P&I Club policies.

The State of Virginia enacted legislation which requires the operator of any tank vessel entering Virginia waters to deposit, with the State, cash in the amount of $500 per gross ton of the vessel. In lieu of the cash deposit, a tank vessel operator may provide evidence of financial responsibility. Financial responsibility may be demonstrated by self-insurance, insurance, guaranty or surety, or any combination thereof. The Virginia statute provides that direct action may be brought against the insurer, guarantor, or surety for violations of the law up to the amount insured, guarantied, or otherwise pledged.

Virginia regulators have interpreted this Virginia statutory requirement to mean that the direct action provision is required only when an instrument of insurance, guaranty, or surety is itself used as the form of financial responsibility. Contrary to the view taken by the State of California, the Virginia State Corporation Commission determined that P&I Club membership was not "insurance" under State Corporation law. As a result, Virginia accepts membership in a P&I Club as evidence of financial responsibility under its oil pollution statute, but without a right of direct action against a Club because, if a

Club is not an insurer, the direct action requirement is a moot point. Additionally, unlike OPA 90, the Virginia law does not define "guarantor" to encompass any entity, other than the responsible party, that provides evidence of financial responsibility for a responsible party. Instead, the Virginia statute specifically defines the types of financial responsibility that are subject to direct action - insurance, guaranty, or surety.[107]

2. Analysis

As mentioned above, this "membership in a P&I Club approach," either as an asset for purposes of calculating net worth and working capital under the self-insurance method,[108] or under any other variation, such as "other evidence," has only one objective -- to enable the Clubs to avoid OPA 90's direct action mandate. However, the primary objective of OPA 90's financial responsibility regime is to guarantee the exact opposite: that the Federal Government and other claimants have assurance that the vessel owner, operator, or guarantor can and will have funds to pay costs and damages at least up to the liability limits set forth in the statute. Under the rule, the Coast Guard is virtually assured that the responsible party and/or the guarantor will have the funds readily available to meet these liability

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[107]Dyer, Ellis, Joseph & Mills, Comments on Notice of Proposed Rulemaking for Financial Responsibility for Water Pollution (Vessels), January 24, 1992, pp. 8 & 9.

[108]A variation of this approach is simply to consider P&I Club membership as an alternative form of "self-insurance." The effect is the same as the membership-as-an-asset approach.

limits. Acceptance of P&I Club membership as an asset, to enable the insured to meet the self insurance requirements of the proposed financial responsibility regulations, would diminish that assurance and expose the OSLTF.

The Coast Guard, and Federal Maritime Commission before it, have always construed "assets" to be those which are attachable, in the United States, by claimants. The face value of insurance, other than prepaid premiums, is not considered an asset under Generally Accepted Accounting Principles ("GAAP") or any other known accounting principles. Because both straight commercial insurance and P&I Club rules provide for a host of policy defenses and other exclusions, there is no assurance or even any promise that the face amount of the policy will be made available. This is not evidence of financial responsibility. Moreover, because of the pay-to-be-paid rule,[109] a Club member does not have the right to demand payment by a Club to a claimant. Hence, P&I membership is not considered an asset in the self-insurance equation in the rule.

Without direct action, due to P&I Club rules, such as the pay-to-be-paid rule, the P&I Clubs will be under no legal obligation to pay claimants for costs and damages associated with

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[109]P&I Club insurance is not straight insurance. It is indemnity insurance, which means that a P&I Club is under no obligation to pay one of its members unless that member pays the claim first out of its (the member's) own pocket. If the liable member is unable to pay out of its own pocket, e.g., if it is insolvent, has declared bankruptcy, or its only asset, the vessel, is on the bottom, the Club is under no obligation to pay the claim.

an oil or hazardous substance spill. Claimants would have no guaranty that the P&I Clubs would not invoke policy defenses with the result being that the responsible party may not have resources or may be willing to bankrupt itself to avoid compensating damaged parties. This same result could occur under the state financial responsibility systems cited above as precedent.

A fundamental purpose of OPA 90 is to ensure that the polluter pays. Should, for whatever reason, a P&I Club elect not to compensate a claimant for damages resulting from a spill, the OSLTF may be required to provide that compensation and may not be able to obtain recovery through subrogation if the responsible party has little or no actual, attachable assets. The P&I insurance-as-an-asset alternative may also force the responsible party to liquidate assets, if any, and possibly cease operations if the P&I Club elects to follow its rules and does not pay.

Under this approach then, there is a serious concern that responsible parties may not be able to pay for costs and damages resulting from an oil spill. Society may then be obligated to pay those costs, impairing an important objective of OPA 90 -- internalization of pollution costs. This option, if adopted, also would discriminate in favor of vessel operators who are members of P&I Clubs and against operators who insure through commercial insurers. Therefore, adoption of this approach may well be challenged by either shipowners insured by traditional insurers or their insurers or both.

3. OSLTF Assigned as a "Loss Payee"

Several commenters to the PRIA suggested a variation to the P&I Club membership-as-an-asset approach.[110] Under this modified approach, the OSLTF would be named a "loss payee" under a P&I Club policy. This approach is intended to allow the government, as the manager of the OSLTF, to stand in the shoes of a vessel owner or operator when, for whatever reason, it fails to pay oil pollution claims and cleanup costs. There is a provision in P&I insurance contracts which allows for the establishment of an assignee or "loss payee". As a "loss payee", the OSLTF could pay private third party oil pollution claims, and then would seek possible reimbursement from the responsible party's P&I Club up to the financial responsibility amount.

The assignment provision has been available, for limited use, for many years. It is traditionally used by banks that have loaned money to vessel owners. Should the vessel owner default on the loan, the bank is in a better position to obtain its loaned money directly from the P&I Club in the form of payments that would otherwise go to the vessel owner.[111]

Under the loss payee approach, the P&I Clubs would still retain the same policy defenses that they would have if they were

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[110]The Coalition of Eight American Companies are the chief advocates of the option. See Coalition of Eight PRIA Comments.

[111]Despite this arrangement, in recent years many lenders have purchased mortgagee insurance to protect their investment. BankAssure is a leader in this insurance product. See Nicholson Chamberlain Colls BankAssure Ltd., Comments on the Preliminary Regulatory Impact Analysis, September 20, 1993, p. 5.

dealing directly with the vessel owner or operator. Also, the "paid-to-be-paid" rule would not be waived. Thus, the "loss payee", in this case the Federal Government, would first be required to process and pay any oil pollution claims and cleanup costs not paid by the responsible party, and then submit a bill to the P&I Club for consideration of payment. In addition, any liabilities of the vessel owner or operator to the P&I Club could first be deducted by the P&I Club before payment of a claim submitted by the "loss payee".

The P&I Clubs would also have to give their consent to the OSLTF becoming a "loss payee".[112] There is some indication they may not give their consent due to fear that the courts will look behind this arrangement and consider the P&I Club an OPA 90 guarantor based upon allowance of the assignment and other actions of the P&I Club, such as submission of information to the Coast Guard concerning entry and termination of entry of the member. In addition, P&I Club rules prohibit members form using entry in a P&I Club as evidence of financial responsibility under OPA 90.

Even if the P&I Clubs would allow the OSLTF to become a "loss payee", without direct action the P&I Clubs will be under no legal obligation to reimburse the OSLTF for the payment of private third party oil pollution claims that the Fund has paid.

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[112]Submitted to the COFR Docket is a letter written by the International Group of P&I Clubs to the American Petroleum Institute which indicates that the International Group has yet to support the "loss payee" assignment.

As is the case with accepting membership in a P&I Club as an asset, the Clubs could invoke policy defenses with the result being that the OSLTF is left footing the bill.[113] This would most likely be the case if the responsible party has little or no attachable assets. Without direct action, there is no assurance that the polluter pays principle would be guaranteed, as required by OPA 90.

It is uncertain if vessel owners would incur any additional costs under the membership-as-an-asset or loss payee approaches. The P&I Clubs have not indicated whether shipowners would be assessed a surcharge assuming the Clubs were willing to agree to the OSLTF becoming a "loss payee". In addition to providing no assurance or even a promise that the polluter will pay pollution claims, the "loss payee" variation may increase costs for oil consumers through higher payouts by the OSLTF and Superfund should a P&I Club deny claims and the responsible party, for whatever reason, does not pay. Thus, it may necessitate the continuation of the collection of oil taxes. Also, additional costs would be incurred by the OSLTF because the Federal Government would first have to adjudicate claims that would otherwise be processed by the responsible party's insurer. As in the case with using P&I Club membership as an asset, this option

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[113]Under similar trust funds, such as CERCLA, Congress expects the Environmental Protection Agency, the manager of the trust fund, to recover cleanup costs from the responsible parties. See House Subcomm. on Investigations and Oversight of the Comm. on Public Works and Transportation, 103d Cong. 1st Sess., Administration of the Superfund Program 27 (Comm. Print 1993).

distinguishes between P&I Clubs and traditional insurers, and could be contested by either shipowners insured by traditional insurers or their insurers or both.

D. ADJUST SELF-INSURANCE FORMULAS

1. General Discussion

The interim rule permits a vessel operator with a specified level of attachable United States assets to self-insure in order to establish financial responsibility. To self-insure, the applicant must establish, by an audit of an independent certified public accountant, that it maintains, in the United States, working capital and net worth in amounts at least equal to the total amount of financial responsibility required under OPA 90 and CERCLA.[114] Another method to demonstrate financial responsibility is through a financial guaranty. This allows a vessel operator to meet the financial responsibility requirement by having any other firm, usually an affiliated company, comply with the self-insurance method on behalf of the vessel operator. Both these methods are currently available under the present financial responsibility regulations.

As of Fall 1993, only two percent of all COFRs issued by the Coast Guard were backed by self-insurance or a financial

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[114]Net worth, as defined in the rule, is the amount of all assets located in the United States, minus worldwide liabilities. Working capital is defined as the amount of current assets located in the United States, less all current worldwide liabilities. The working capital test is routinely waived for financially stable operators who meet the net worth test, if a waiver is requested.

1994 and open for public comment. It defined the issues and elicited several hundred comments.

All issues now have been aired, and the Coast Guard has decided that in the essence of the NPRM, subject to technical changes adopting many of the commenters' suggestions and, in particular, alleviating the comments that P&I Clubs and other guarantors could somehow become subject to unlimited liability. These changes are identified in the discussion that follows. The Coast Guard has decided on this course of action because it believes that the central objections of the commenters to the rule are objections to OPA 90 itself (for example, potential unlimited liability of vessel owners and operators), and, if necessary, should be dealt with by the Congress and not the Coast Guard. The central issue germane to this rulemaking is whether owners and operators will be able to obtain financial responsibility guaranties if the P&I Clubs, as they have declared, do not provide guaranties of insurance. From the letters submitted to the regulatory docket, the Coast Guard concludes that even if the P&I Clubs do not provide these guaranties, alternative financial responsibility sources will be available. These include commercial insurance entities and surety bond companies, as well as the potential greater use of self-insurance and financial guaranties. These alternatives are described more fully in the final regulatory impact analysis (RIA) that accompanies this rule, a summary of which appears under the heading "Regulatory Impact Analysis", in this preamble. The Coast Guard has determined that the approach in the NPRM best fulfills the intent of Congress to assure prompt and certain compensation by the polluter to victims of oil spills and hazardous substance releases. Other suggested alternatives do not satisfy that intent. Among these alternatives are: treating P&I Club membership as an asset for self-insurance purposes; treating P&I Club membership, with a provision making the Oil Spill Liability Trust Fund a "loss-payee," as a form of self-insurance; and adoption through legislation of a "Mandatory Excess Insurance Facility." These alternatives are discussed in detail in the final RIA accompanying this rule. The alternatives have not been adopted. That was the main issue in this proceeding. The other issues primarily concern specific technical aspects of each section of the rules.

Part and Section Numbers

The NPRM proposed that preexisting part 130 be replaced by a completely new part 138, that parts 131 and 132 be removed, and that subpart D of part 137 be removed and reserved. In order to cause as little disruption to the maritime industry, an orderly compliance schedule is being adopted. This schedule allows existing Certificates for non-tank vessels to be used until their regularly scheduled expiration dates, as described in the section of this preamble labeled, "Implementation Schedule." Because of this phased approach, preexisting parts 130, 131, and 132, and subpart D of part 137, must temporarily remain effective after the effective date of this rule. Accordingly, a new part 138 has been designated for the rule that will replace preexisting parts 130, 131, and 132, and subpart D of part 137. Conforming amendments have been made to 33 CFR parts 130, 131, and 132, and subpart D of part 137. The following table shows the location in the new part 138 of the corresponding sections of the NPRM:

NPRM Part 130	Part 138
130.1(b)	138.10.
130.1(a); 130.2(b) ("vessel").	138.12.
	138.15 (new).
130.2	138.20.
130.3	138.30.
130.4	138.40.
130.5	138.50.
130.6	138.60.
130.1(c)	138.65.
130.7	138.70.
130.8	138.80.
130.9	138.90.
130.10	138.100.
130.11	138.110.
130.12	138.120.
130.13	138.130.
130.14	138.140.
130.15	138.150.
Appendix A	Appendix A.
Appendix B	Appendix B.
Appendix C	Appendix C.
Appendix D	Appendix C.
Appendix E	Appendix E.
Appendix F	Appendix F.
Appendix G	138.80(f).

Implementation Schedule

Section 1016(h) of OPA 90 (33 U.S.C. 2716(h)) states that financial responsibility regulations under acts repealed or superseded by OPA 90 remain in effect until superseded by new regulations issued under OPA 90. Therefore, the financial responsibility requirements in 33 CFR part 130 (FWPCA), 33 CFR part 131 (TAPAA), 33 CFR part 132 (OCSLAA), and 33 CFR part 137, subpart D (DPA) will remain in effect with respect to individual vessels in the manner prescribed by section 138.15 of this rule. The intent of the implementation schedule (which could also be termed a compliance schedule) is to allow for an orderly transition to part 138 by allowing, as some commenters recommended, COFRs issued under the preexisting regulations to remain valid up to their expiration dates. The Coast Guard is affirming that comment, but only with respect to non-tank vessels. (As explained below, tank vessels will be required to demonstrate financial responsibility under the new part 138 on a more expedited schedule.) This phased-in transition will also enable the Coast Guard to issue new Certificates in an orderly manner utilizing existing resources. Rather than attempting to issue approximately 23,000 new COFRs by a single, mandatory date, the Coast Guard expects the future Certificate renewal cycle, applicable to Certificates issued under this rule, to result in the renewal of about one-third that number each year. No new Coast Guard resources would be required for that routine renewal cycle.

The existing operators of non-tank vessels which presently are subject to the regulations issued under one or more of the preexisting CFR parts may continue to comply with those preexisting regulations for, in some cases, three and one half years after publication of this rule in the **Federal Register**, depending upon the expiration dates of their preexisting COFRs. These operators also have the option of choosing to comply with this rule soon after its initial implementation date, which is 180 days after the publication date, i.e., "effective date".

On the other hand, self-propelled tank vessels, followed by non-self-propelled tank vessels, will be required to comply with this rule sooner than non-tank vessels because of the generally greater danger of large and possibly catastrophic spills from tank vessels. Self-propelled tank vessels will be required to submit, not later than 180 days after publication of this rule in the **Federal Register**, at least the evidence of financial responsibility required by this rule (new application forms will be required later). Non-self-propelled tank vessels (i.e., tank barges) will be required to submit, not later than one year after publication of this rule in the **Federal Register**, application forms as well as evidence of financial responsibility required by this rule.

Although this phased transition to the new rule may appear complicated it is designed to impose the least burdensome requirements on the regulated community while balancing the need of potential claimants to be assured that the vessels posing the

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 9
COFR HEARING, 21 JULY 94

QUESTION. WHAT HAS BEEN THE ROLE OF INSURANCE COVERAGE BY P&I CLUBS WITH RESPECT TO REMOVAL COSTS AND DAMAGE LIABILITY PRIOR TO AND UNDER OPA-90? WHO WAS ELIGIBLE TO FILE CLAIMS AGAINST A RESPONSIBLE PARTY OR GUARANTOR PRIOR TO AND UNDER OPA-90?

Answer. The P&I Clubs have provided in the past, currently provide, and have stated they will continue to provide, insurance coverage for oil spills under U.S. law. In addition, P&I Clubs provided evidence of financial responsibility under former section 311(p) of the Federal Water Pollution Control Act (FWPCA) and under the Trans Alaska Pipeline Authorization Act. Under the FWPCA, the financial responsibility provider was subject to direct action by the federal government. Under the TAPAA, direct action was available to any damaged party.

The Clubs also provide guaranties under the international Civil Liability Convention (CLC), and consent to claims from all parties. Under both the TAPAA regulations and the CLC, a guarantor is precluded from invoking policy defenses.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 10
COFR HEARING, 21 JULY 94

QUESTION. HAS THERE BEEN ANY TIME, TO THE COAST GUARD'S KNOWLEDGE, THAT P&I CLUBS HAVE NOT PROVIDED THE COVER TO ITS LIMIT FOR AN OIL SPILL?

Answer. A few times over the past 24 years, the United States has had to litigate in order to secure payment, but those few cases involved novel issues and do not represent the reliability of P&I Clubs as guarantors. Overall, the Clubs' record is outstanding. The Clubs, insofar as claimants are concerned, voluntarily acted like OPA 90 guarantors before there was an OPA 90, and they continue to do so today, despite what may be said technically for the record. The Coast Guard's perception of the Clubs is based on a long-standing relationship of trust and respect, but the explicit wording of OPA 90's guarantor provisions results in our current requirement of written guaranties.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 11
COFR HEARING, 21 JULY 94

QUESTION. IF THIS RULE HAD BEEN IN EFFECT, WHAT PERCENTAGE OF THE ACTUAL REMOVAL COST AND DAMAGES WOULD IT HAVE COVERED IN THE EXXON VALDEZ INCIDENT AND THE MORRIS J. BERMAN INCIDENT?

Answer. The rule would have required Exxon to have established $114 million worth of evidence of financial responsibility. The pre-OPA 90 rule (33 CFR 131) required evidence of financial responsibilty only in the amount of $14 million.

In the MORRIS J. BERMAN spill, we estimate that this rule's requirement of evidence of financial responsibility of $10 million would have assured payment of just over 10% of the costs and damages. If, however, the guarantor was able to utilize a defense to liability, e.g., willful misconduct of the vessel operator, this rule would have had no effect. That, of course, is the reason why U.S. taxpayers and consumers contribute to the backup Oil Spill Liability Trust Fund.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 12
COFR HEARING, 21 JULY 94

QUESTION. HAS THE COAST GUARD INVESTIGATED THE VARIOUS METHODS ADOPTED BY STATE GOVERNMENTS AS WAYS TO PROVIDE THE EVIDENCE OF FINANCIAL RESPONSIBILITY THAT MIGHT ALLOW THE P&I CLUBS TO CONTINUE TO PROVIDE COVERAGE BUT NOT BE GUARANTORS? (I.E. CALIFORNIA, WASHINGTON, ETC.)

Answer. Yes. The Coast Guard looked at these options, but concluded that OPA 90 does not provide the flexibility allowed by state laws. The discussion in the Regulatory Impact Analysis pages 88-91 (attached) amplifies our conclusion.

(See attachment to question 8.)

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 13
COFR HEARING, 21 JULY 94

QUESTION. WHAT HAPPENS IF AN INSURANCE ENTITY PAYS SEVERAL CLAIMS THAT CAUSES IT TO FALL OUT OF COMPLIANCE WITH THE STANDARDS REQUIRED TO MEET APPROVAL? WILL THE COAST GUARD SUSPEND OR REVOKE THE COFRS THAT THE ENTITY ISSUED?

Answer. The Coast Guard's COFR guarantor approval standards are designed to make such an event highly unlikely. The Water Quality Insurance Syndicate, Lloyd's Underwriters and the member companies of the Institute of London Underwriters are examples of commercial guarantors who routinely pay numerous claims without causing their financial conditions to fall below an acceptable standard. Only once during the 24 year history of this program did claims payouts cause the solvency of an approved guarantor to fall below our standards. In 1984, a P&I Club lost the backing of its reinsurers because of the alleged failure of the Club to make a material disclosure to the reinsurers when the reinsurance was being purchased. The Club, therefore, had to pay claims out of its own reserves and soon became insolvent. The Coast Guard was forced to write to all of the involved vessel operators and instruct those operators to obtain acceptable, substitute guaranties by a certain date. Failure to do so would have resulted in the revocation of the operators' COFRs. Accordingly, the involved vessel operators changed guarantors.

CONGRESSMAN TAUZIN QUESTIONS
WITH COAST GUARD ANSWERS: 14
COFR HEARING, 21 JULY 94

QUESTION. IF A VESSEL OWNER ACQUIRES A SURETY BOND TO GET A COFR, WHO WILL SERVICE THE CLAIM IN CASE OF A SPILL? WHO WILL BE THE PARTY THAT RECEIVES THE BOND AND WHO DECIDES THE PRIORITY AND APPROVAL OF CLAIMS?

Answer. A surety company providing a surety bond guaranty is like any other "guarantor." Claims may be filed directly against that guarantor (surety company), and that guarantor will be expected to process those claims. Except as otherwise provided in OPA 90, all claims must be presented first to the responsible party or guarantor before presentment to the fund. If each person to whom the claim is presented denies all liability for the claim, or it remains unsettled after 90 days, the claimant may elect to submit the claim to the fund. OPA 90 does not specify the order in which a guarantor (or responsible party for that matter) pays claims. On the other hand, the Internal Revenue Code provides that if claims exceed the balance in the Oil Spill Liability Trust Fund, those claims shall be paid by the Fund in full in the order in which they were finally determined. 26 U.S.C. 9509(e)(3). A guarantor receiving claims is responsible for deciding the priority and approval of claims received by that guarantor.

It might develop that the surety companies will receive few if any direct claims. The responsible party's P&I Club or other insurer may wish to pay claims. Only in those circumstances in which the insurer refuses to pay, because of policy defenses or for other reasons, is the surety likely to receive direct claims.

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CONGRESSMAN BARLOW QUESTIONS
WITH COAST GUARD ANSWERS: 1
COFR HEARING, 21 JULY 94

QUESTION. WHY HASN'T THE COAST GUARD PUBLISHED THE CRITERIA BY WHICH INSURANCE COMPANIES WILL BE JUDGED "ACCEPTABLE" TO THE COAST GUARD?

Answer. The criteria has been much the same for the last 24 years and has been available to anyone who inquired. Also, because the P&I Clubs and other established guarantors provided the backing for almost all vessel operators wishing to evidence their financial responsibility, we did not believe another Federal regulation was necessary.

CONGRESSMAN BARLOW QUESTIONS
WITH COAST GUARD ANSWERS: 2
COFR HEARING, 21 JULY 94

QUESTION. WHAT ARE THE CRITERIA FOR FINDING INSURANCE COMPANIES ACCEPTABLE?

Answer. With respect to insurance companies, we consider each prospective guarantor's approval as an agency adjudication where each case is determined on its own merits, given the totality of the circumstances. The following criteria are used in our determinations:

a. The first criterion is that prospective guarantors must be financially sound and be able to write risks at the intended level. In the case of stock companies, our general policy with respect to tankships is not to allow retained risks exceeding approximately 5 percent of policyholder surplus or 10 percent of policyholder surplus in the case of non-tankships. In the case of true mutuals, such as the International Group of Protection and Indemnity Clubs, "policyholders surplus" can be a relative term because of the ability of mutuals to call upon their members for additional funds, as needed. Therefore, our policy is flexible concerning the amount of risk on particular undertakings.

b. The second criterion is that a prospective guarantor must participate in a sound reinsurance program, as implied in the above discussion of the first criterion.

c. Other criteria are: willingness to provide financial reports; government oversight at the place domiciled; appointment of a United States agent for service of process; and an unblemished record concerning any previous guaranties filed with the Coast Guard.

An insurer is automatically assumed to meet the first two criteria mentioned above if the insurer has been awarded a "B" or better rating by the well-known professional insurance rating organization, A. M. Best, and has a Best's financial rating commensurate with the size of the net risk the prospective guarantor intends to retain. Our criteria, although probably more strict than other agencies, has been consistently applied for many years and is based on criteria established by the Maritime Administration, Federal Maritime Commission and A. M. Best. This is, however, an area of regulation where the Coast Guard has some flexibility, and the Coast Guard is mindful of the language in OPA 90's Conference Report concerning one of OPA 90's section 1016 objectives: fostering a continuing market for guarantors.

CONGRESSMAN BARLOW QUESTIONS
WITH COAST GUARD ANSWERS: 3
COFR HEARING, 21 JULY 94

QUESTION. WHAT MECHANISM DOES THE COAST GUARD ENVISION FOR MONITORING THE COFR APPLICATIONS THAT ARE RECEIVED?

Answer. The Coast Guard's National Pollution Funds Center maintains a computer-based COFR data base which we will utilize for this purpose.

CONGRESSMAN BARLOW QUESTIONS
WITH COAST GUARD ANSWERS: 4
COFR HEARING, 21 JULY 94

QUESTION. DOES THE COAST GUARD FEEL IT HAS ANY FLEXIBILITY UNDER THE LAW TO CONSIDER SOLUTIONS DEVELOPED BY INDUSTRY?

Answer. As currently written, OPA 90 does not provide the flexibility to allow the Coast Guard to adopt the industry solutions that were advanced during the notice of proposed rulemaking stage of this proceeding. For example, Congress did not empower the Coast Guard to accept P&I Club membership to be a form of financial responsibility without subjecting the P&I Club to guarantor status under OPA 90. Similarly, the Mandatory Excess Insurance Facility solution would require an entirely new legislative approach which is still in its formative stage and which embodies no assurances that either Congress, or industry as a whole, would approve it. Further explanation respecting the incompatibility of the industry proposals with Congressional OPA 90 mandates are contained in the attached excerpts from the Regulatory Impact Analysis (pages 88-97).

(See attachment to question 8 of Mr. Tauzin for excerpts.)

More recently, the insurance and surety industry has been exploring new methods for demonstrating financial responsibility that are in accord with OPA 90. The Coast Guard is considering these methods.

CONGRESSMAN BARLOW QUESTIONS
WITH COAST GUARD ANSWERS: 5
COFR HEARING, 21 JULY 94

QUESTION. WHAT WILL YOU DO IF THE SPECIALTY INSURERS FAIL TO EMERGE AS ANTICIPATED?

Answer. We have stated before that we have not placed all our eggs in one basket-- we believe a mix of opportunities for compliance will exist. Presently, the market is reacting to the need for evidence of financial responsibility in light of the P&I Clubs' refusal to issue OPA 90 guaranties. Companies are looking at self-insurance or financial guaranty options, surety companies are busily developing and marketing surety bond guaranties, WQIS is expected to provide financial responsibility guaranties for the inland and small coastal fleet, and we understand that both Shoreline Mutual and First Line are diligently working to finalize their arrangements. We have heard rumors of other companies quietly working on financial responsibility products, and hundreds of insurers around the world could choose to issue OPA 90 guaranties.

BEFORE THE

SUBCOMMITTEE ON COAST GUARD AND NAVIGATION

COMMITTEE ON MERCHANT MARINE AND FISHERIES

HOUSE OF REPRESENTATIVES

STATEMENT OF

TERENCE G. COGHLIN,

CHAIRMAN OF

THE INTERNATIONAL GROUP OF P&I CLUBS,

ON THE UNITED STATES COAST GUARD

INTERIM RULE ON

CERTIFICATES OF FINANCIAL RESPONSIBILITY

UNDER THE OIL POLLUTION ACT OF 1990

21st JULY, 1994

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My name is Terence Coghlin, Chairman of the managers of The U.K. P&I Club. I appear here today as the Chairman of the International Group of P&I Clubs (the "Group") on behalf of the member Clubs of the Group. I am accompanied today by Lloyd Watkins, Secretary and Executive Officer of the Group and Robert Seward, a partner in Tindall, Riley and Company, managers of the Britannia PandI Club.

I. INTRODUCTION

The P&I Clubs are privileged to appear before this Subcommittee to provide their views on certification of financial responsibility under the Oil Pollution Act of 1990 ("OPA 90" or the "Act"). The matter of certification was the subject of a previous hearing held by this Subcommittee on 6th November, 1991 concerning the Coast Guard's then recently issued Notice of Proposed Rulemaking ("NPRM"). At that hearing, the Subcommittee received testimony from the Clubs and representatives of the marine insurance and shipping industries which was unanimously critical of the approach to certification reflected in the NPRM. The essence of this criticism was that the approach was unnecessarily narrow and rigid, and that, if the certification requirement were to be implemented in the manner proposed in the NPRM, few shipowners would be able to comply with that requirement.

Today's hearing is occasioned by the publication on 1st July, 1994 of the Coast Guard's Interim Rule concerning certification, and accompanying Final Regulatory Impact Analysis ("FRIA"). Regrettably, the Coast Guard has failed to take proper account of the concerns we and others have raised concerning the approach to certification embodied in the NPRM, and has instead published an Interim Rule under which the certification requirement of OPA 90 would be implemented in a manner virtually the same as that contemplated in the NPRM. It is a course which we believe is based on a misunderstanding of the reasons for enactment of OPA 90 and the very real practical benefits of the P&I Club system.

It must be remembered that OPA 90 was <u>not</u> enacted to address a perceived crisis concerning the availability or adequacy of insurance cover for U.S. oil pollution risks. There was no insurance crisis involved with the EXXON VALDEZ spill. The covering P&I Club met its policy obligations in full -- to the tune of $400 million. Indeed, prior to and since the passage of OPA 90, the Clubs have provided insurance cover wide enough and more than sufficient in amount to meet the financial responsibility requirements of OPA 90, and they have met in full their obligations

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under that cover whenever a spill has occurred. The Clubs' insurance cover is backed by more than sufficient assets and supported by a unique reinsurance policy written on terms which ensure the ability of the system to provide the breadth and amount of oil pollution cover which the Clubs offer, including the ability to support shipowner liability for any number of claims in a given year. The value of this system to shipowners and claimants has been demonstrated repeatedly in every oil spill in United States waters in which the Clubs have been insurers. In each of these spills, the Clubs have responded fully under the terms of their cover, thereby enabling the shipowner to clean up the spill and compensate those damaged by it. None of these spills has revealed any inadequacy in the P&I Club insurance system.

Despite this exemplary record, the Coast Guard has now adopted a narrow approach to certification which fails to give proper weight to the tried and tested P&I Club system -- a system which the Coast Guard itself referred to in its FRIA as a "logical and time-tested concept" for coping with the consequences of oil spills. See FRIA, at 31. Consequently, the Coast Guard has been led to propose reliance upon a new system consisting of entities which have never before provided pollution cover, but which have now expressed their ability and willingness to issue the guaranties which would be required under the Interim Rule. The Coast Guard also refers to unnamed and unknown commercial insurers who may or may not come forward but does not identify any insurers with significant experience in handling substantial risks of this magnitude and complexity.

It is of course possible that there are other underwriters who may be able to satisfy the Coast Guard's view of the financial responsibility requirements of OPA 90, but there is good reason for the Coast Guard and shipowners to proceed cautiously before relying on any unproven proposals to provide certification. It is not yet clear which of these entities will be willing and able to provide cover beyond the liability limits of OPA 90. Such cover is also apparently to be offered at a cost greatly in excess of what shipowners are now paying under the P&I Club system for cover which is much broader in scope and higher in amount.

Moreover, the record contains no evidence that any of the entities which have expressed a willingness to provide certification actually possess the necessary capital or reinsurance backing, particularly bearing in mind the possibility of multiple spills.

If the Interim Rule remains as it is and if, as the Coast Guard maintains, there are sound underwriters prepared and able to provide the required guarantees, the Clubs' position will not alter for the reasons already stated and further explained in section II below. It should be recalled that the Clubs have stated and maintained their position on the fundamentally different guarantees required by OPA 90 since before that act was passed and the present crisis is not of their making, but rather created by the Coast Guard's refusal to heed the warnings given by Chairman Tauzin at the Subcommittee's 6th November, 1991 hearing on certification.

II. THE BASIC POSITION OF THE CLUBS

The Clubs' previous comments concerning the NPRM are equally applicable to the Interim Rule which closely follows the approach to certification proposed in the NPRM. It is appropriate therefore for us only to restate briefly here some of what we have said before concerning the Clubs' position in respect of oil pollution cover and certification.

In their formal statement and testimony at the prior hearing and in comments to the Coast Guard, the Clubs restated

their longstanding position that they can not become guarantors under OPA 90. However, the Clubs also stated their belief -- a belief shared by the vast majority of those who have submitted their views on the subject -- that, by making use of the flexibility Congress had expressly given the Coast Guard in the Act, the Coast Guard could fashion a regulation which would enable shipowners to utilize their P&I Club cover to establish financial responsibility without requiring the Clubs to become guarantors. The Congress gave the Coast Guard such flexibility in order to "foster a continuing market for providers of financial responsibility." The Clubs are disappointed that the Coast Guard did not utilize this flexibility.

A. P&I Club Oil Pollution Cover

The Clubs are mutual, non-profit organizations which together insure a large percentage of the world's oceangoing fleet, including virtually all ocean going oil tankers and dry cargo ships. The Clubs currently provide oil pollution cover which is more than sufficient in scope and amount to meet the financial responsibility requirements of OPA 90. The Clubs would like to be able to continue to make available such cover with respect to vessels trading to the United States (although whether the Clubs will be able to continue to do so after the Natural Resource Damage Assessment system has been fully developed remains to be seen).

B. Certification

The Clubs have repeatedly stated that they are not in a position to provide certification under OPA 90. As the Clubs declared previously to this Subcommittee:

> "This is not, Mr. Chairman, because of any single provision in the Act or in the proposed regulations but because the Clubs consider as responsible insurance companies that the overall effect of OPA 90 is to undermine the very basis of the clubs' insurance cover. Each club is being asked to depart from its normal and well-understood role as indemnity underwriter for named shipowners throughout the world and to expose itself as a guarantor, without policy defenses and possibly without financial limit, to a multitude of unknown potential claimants and in respect of strict liability for damages of unprecedented size and scope.
>
> "This is a situation which puts at risk the whole worldwide P&I structure including the reinsurance program upon which the Clubs depend so heavily and all to support an Act which represents a unilateral departure by the United States from the process of further development of international lawmaking in the pollution field."

This is why the Boards of Directors of each of the Clubs decided not to expose the Clubs to liability as a guarantor. Since the Interim Rule was published on 1st July, 1994, all of the Clubs who have held Board meetings have reconfirmed this position.

III. RESPONSE TO ISSUES RELATING TO CERTIFICATION AND THE CLUBS CONTAINED IN THE INTERIM RULE AND FRIA

While our previous comments address the basic issues presented in the Interim Rule and the FRIA, the Clubs would like to

take this opportunity to address certain issues concerning certification and the Clubs which are contained in these documents.

A. Certification Under OPA 90 Is Fundamentally Different From The Certification The Clubs Currently Provide Under the Clean Water Act and Civil Liability Convention

The Interim Rule and FRIA state that certification of financial responsibility under OPA 90 is similar to the certification of financial responsibility already provided by the Clubs under the Clean Water Act or the Civil Liability Convention ("CLC"). This statement is incorrect. The liabilities imposed under OPA 90 are significantly different both in the amount and the scope of damages which can be recovered. So too are the obligations of a guarantor.

- If the Clubs were to become guarantors under OPA 90, they could be directly exposed to double jeopardy by the interaction of federal and state statutes in respect of virtually each and every government and private claim for compensatory damages, including speculative claims for natural resource damage, and possibly also exposed to punitive civil penalties or even criminal sanctions.

- By contrast, the obligations of a guarantor under the Clean Water Act are not only restricted to a significantly lower financial amount but also, even more importantly, they are confined to a single entity, the Federal Government and a single category of claim, namely costs of clean-up and restoration.

- Although the CLC includes within its scope claims for compensation by private parties, the Convention enshrines both the right of the registered owner (the sole "responsible party"), to limit his liability in the absence of his "actual fault or privity", and the mechanism whereby that limitation can be assured, namely the establishment of a limitation fund in a single competent court. The guarantor can avail himself of the right to establish a limitation fund and thus discharge his full liability.

- In contrast, guarantors under OPA 90 may be sued in several different state and federal courts and may be held liable up to the limit certified, and possibly beyond, in each court. Moreover, as OPA 90 prescribes no system under which a guarantor may prorate its liability limit in paying claimants in several different court actions, a guarantor which decides to pay claims asserted in one court action, but not claims asserted in another case, could be exposed to claims they engaged in improper preferences among claimants. The absence of a mechanism under OPA 90 for a guarantor to discharge its liability through the use of a single limitation fund therefore makes illusory the limit of liability provided for guarantors under section 1016(g) of the Act.

- The Coast Guard refers also to other federal acts (TAPAA, DPA, OCSLA, and CERCLA) which require evidence of financial responsibility. It is significant that all of these acts are modest in amount, particularly when compared to OPA 90. In addition, with the exception of CERCLA, all of

these acts are limited in scope. With respect to CERCLA, the broadest of the acts, its financial responsibility requirements have never been put into effect by regulation, notwithstanding the act was passed more than 12 years ago. It is important to note that the principal reason why the financial responsibility requirement of CERCLA has never been implemented is that no guarantor or insurer has expressed a willingness to cover these liabilities.

- As guarantors under OPA 90 would be subject to multiple direct lawsuits by anyone or any entity asserting a claim, such guarantors would be confronted with the prospect that their own conduct, rather than that of the responsible party, could become the central issue in trials that should be about the pollution incident. Guarantors may well find that the manner in which they prioritize and pay these claims may be the subject of second-guessing by state and federal courts and may result in liability under theories of "insurance bad faith," separate and apart from that which they face pursuant to the Act.

The suggestion in the FRIA that the financial responsibility requirements of OPA 90 are merely a continuation of a legislative tradition already well accepted by the P&I Clubs, ignores completely the fundamental differences in OPA 90 which lie at the root of the P&I Club's decision not to become guarantors under OPA 90.

B. The Clubs Have A Legitimate Concern That Their Reinsurance Contract Could be Jeopardized by Assuming Guarantor Status Under OPA 90

The Clubs' reinsurance contract covers worldwide P&I liabilities of all types, not merely pollution risks or risks in any one country. As such it is one of the biggest liability contracts in the world. As stated in the Group's submission in response to the NPRM: "There is no alternative reinsurance market."

It is significant that Lloyd's of London provide a substantial proportion of this reinsurance. This is not a matter of choice on the part of the Clubs but one of necessity since major insurers elsewhere in the world are reluctant to participate in the risk at all. This is not because of price but because of the exposure the contract gives in particular to pollution risks and liabilities in the United States. By way of example, the current participation of insurers in the United States is less than 7 per cent. The Clubs' search for other untapped capacity elsewhere in the world has been unsuccessful.

The Coast Guard, in its FRIA, has pointed out that under OPA 90, "all of Lloyd's and other reinsurers' $470 million plus all of Lloyd's excess $200 million is potentially at greater risk" than under the 1969 CLC. FRIA, at 32. The Coast Guard also explains that "[p]ursuant to OPA 90, Lloyd's can expect to pay out substantially more for claims in the United States than it will under the 1969 CLC exposure for the rest of the world." Id., at 33.

It will be readily appreciated then that the issue is not one of cost but of willingness to participate at any price. In view of the importance to the Clubs of their worldwide reinsurance contract and the current difficulties being experienced in preserving this reinsurance contract as a whole for the benefit of all the members of each of the P&I Clubs, it is inevitable that the P&I Clubs must have proper regard for the preservation of as much reinsurance capacity as is possible.

C. The Clubs Have Not Taken Their Position Concerning Certification In The Belief That the Congress Will Adopt the Protocols

A theme repeated by the Coast Guard in both the Interim Rule and the FRIA is that the Clubs' position concerning certification is an attempt to promote the repeal of OPA 90 and the adoption of the Protocols. The Clubs recognize Congress has not ratified the Protocols; and, while, for the reasons previously stated, the Clubs have always supported and will continue to support the prompt clean-up of spills under international regimes, the Clubs do not anticipate the Congress will suddenly reverse course and adopt the Protocols. In this regard, it is important to note that, despite their disappointment at the passage of OPA as written, the Clubs have not withdrawn cover for oil pollution in United States waters.

The Clubs' position concerning certification and guarantor status was taken relative to the substance of those issues and their effect on the Clubs, their Members and the worldwide P&I Club system.

D. Shipowners Trading to the United States Are Fully Aware Of and Understand the Reasons Why the Clubs Have Declined To Become Guarantors

In both the preface to the Interim Rule and the FRIA the Coast Guard asserts repeatedly that shipowners trading to the United States will require the Clubs to become guarantors. This assumption is misconceived as it ignores the fact that shipowners want to see the integrity of the P&I Club system preserved worldwide. In this regard, strong statements of support of the Clubs' position have been given to the Coast Guard by shipowners, including those trading to the United States, in response to the Coast Guard's Preliminary Regulatory Impact Analysis.

As stated above, the decision not to provide evidence of financial responsibility was made by each individual Club at the level of its Board of Directors or Committee. These Boards or Committees are composed of shipowner representatives of the membership of each Club and are representative of the shipowning community worldwide. There is no basis to assume Board or Committee members would automatically put at risk the worldwide P&I system to address the unique requirements concerning those vessels in the United States oil trade which represent only some of the vessels covered by the Clubs.

IV. CONCLUSION

The final sentence of the FRIA asserts: "Accordingly, the severe economic disruption predicted by the Clubs and their shipowners will not occur without a concerted effort by shipowners to purposefully cause that disruption." This statement is completely unfair and highly prejudicial to the Clubs and their shipowner members. The shipowners have no interest whatsoever in causing such disruption. They and their Clubs have consistently cooperated to the best of their ability with the Coast Guard in seeking to provide the best protection possible to the United States environment. They cannot, however, allow their Clubs to provide financial guaranties which in effect put the whole worldwide P&I insurance structure at risk of destruction.

STATEMENT
OF
J. RICHARD L. YOUELL
BEFORE THE
HOUSE MERCHANT MARINE AND FISHERIES
SUBCOMMITTEE ON COAST GUARD AND NAVIGATION

July 21, 1994

Chairman Tauzin, Representative Coble, and Members of the Subcommittee, thank you for the opportunity to appear before you today, which is the second such occasion for me, the first having been the Subcommittee's November 1991 hearing on the Coast Guard's then-proposed rule on vessel financial responsibility.

I am a marine Underwriter at Lloyd's of London and a Director of Janson Green Ltd., which is an underwriting agency at Lloyd's. Lloyd's is one of the oldest insurance institutions in the world, having begun in 1688. Lloyd's, however, is not a company but a marketplace of some 18,000 individual underwriting members and, beginning with 1994, also certain corporate underwriting members. These underwriting members operate through some 200 syndicates, and I am the principal professional Underwriter for the largest marine syndicate managed by the Janson Green agency.

Because Lloyd's is a marketplace in which each syndicate decides for itself what risks it will accept, there is no one voice which can speak for the whole of the Lloyd's market on any matter of underwriting judgment. Therefore, my remarks today are, strictly speaking, only one Underwriter's view. Nevertheless, as an Underwriter with 29 years' experience at Lloyd's and as a member of several market committees within the Lloyd's community, I believe I can fairly say that my views on guaranteeing financial responsibility under the U.S. Oil Pollution Act of 1990 (OPA) are widely held among marine Underwriters at Lloyd's.

The Lloyd's market collectively is one of the largest sources of insurance capacity in the world, and over its 306-year history it has earned a reputation for innovative and flexible responses to unusual risks, as well as unsurpassed security. Lloyd's pioneered marine oil pollution insurance, and Lloyd's is still one of the world's principal sources for such cover for both offshore production facilities and tankers and other vessels. Indeed, the U.S. insurance market generates virtually no capacity for liability insurance for oil pollution from vessels. London and other non-U.S. markets provide most of the coverage worldwide. We at Lloyd's have every intention of continuing to provide oil pollution insurance for our many insureds, some of whom have been insured at Lloyd's for many years. We would hope to go on providing this insurance for U.S. waters even though the growing multiplicity of liability rules imposed at the Federal and State levels makes this cover increasingly difficult to underwrite.

The Lloyd's market currently make available a layer of $200 million per incident in excess of the $500 million primary cover offered by P&I Clubs to all tanker owners. Lloyd's also are the leading reinsurers (with the greatest participation) of the International Group of P&I Clubs' $500 million pollution coverage program. Although the amount of coverage available at Lloyd's or elsewhere in the world varies from year to year, our capacity at this time is more than sufficient to meet on an indemnity basis the monetary

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limits of the financial responsibility requirements of OPA for vessels and offshore facilities. However, because the vessel owner's limit of liability might be easily breached under OPA Section 1004(c) and further because OPA does not preempt State laws imposing additional liability for the same incident, vessel owners have exposures well in excess of the OPA financial responsibility requirements, which they endeavor to cover with insurance irrespective of the COFR requirements. However, the owner's potential U.S. liability from these cumulative sources is now well beyond the bounds of insurance cover available even if the owner meets the applicable financial responsibility amounts.

Please be assured that we at Lloyd's are in the business of writing difficult classes of insurance, and we take pride in providing our insureds with continuity of coverage even in difficult times. We will continue to provide as much insurance capacity as possible to these insureds. However, we are unable to provide unlimited insurance coverage, because such risk cannot be quantified to determine the appropriate premium, nor can we be sure of our ability to respond, for an unlimited amount, to the promise to pay that is a fundamental element of an insurance contract.

Since your November 1991 hearing a great deal of work and comment has been expended by both the Coast Guard and other parties on the OPA financial responsibility rulemaking. The Interim Final Rule issued earlier this month is an interesting effort by the Coast Guard to respond to the many points of technical suggestion and criticism which were leveled at their original proposal. Certainly, we accept that some of the specific changes made in the Interim Rule were a sincere attempt by the Coast Guard to address particular issues which we at Lloyd's and perhaps others had raised, and to thereby eliminate some of the uncertainty and potentially unlimited liability of guarantors in direct action suits. Unfortunately, however, these changes (in most cases, not the remedy we had suggested) raise as many questions as they seek to answer, and certainly our counsel will be filing technical comments on the specific provisions within the 90 days allowed in the Interim Rule's request for further comments.

While we are still evaluating the legal strength of the guarantor protections offered by the Interim Rule, all of the changes offered to a guarantor's exposure appear to be superficial improvements which do not address the problem head-on. The fundamental difficulty, in our view, remains. Guarantorship under the Interim Rule provides indemnity insurers such as ourselves with a unique challenge, to which we remain unable to respond. Insurers are asked to be alone directly answerable (under OPA Sec. 1016(f)) to a wide-range of claimants for a polluter's conduct, not our own; to advertise the availability of our funds (under OPA Sec. 1014(b)) with unknown liability for getting it wrong and no precedents or guidance about how to "get it right." In a recent Clean Water Act suit, Justice Department lawyers alleged that a mere insurer had an affirmative duty, not only to reimburse the government but to have performed its own cleanup at a remote site. Further, insurers risk being second-guessed about the distribution of limited funds among multiple claimants each conceivably claiming to stand in the shoes of the original policyholder. Finally, insurers are at risk that any number of State and Federal courts all having jurisdiction over OPA actions as a result of OPA Sec. 1017 (b) and (c) could decide the scope of an "incident" differently to circumvent the per-incident limit that is otherwise supposed to protect a guarantor under OPA Sec. 1016(g) against multiple-limits exposure.

The Interim Rule might have attempted to protect a guarantor against any of these consequences affirmatively, but it did not. The Interim Rule does offer two vague[1] new "defenses" to a guarantor (i) against claims in "any court" exceeding the per-incident

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[1] The Insurance Guaranty Form (Form CG-5586) promulgated by the Interim Final Rule provides that "the Insurer shall be entitled to invoke only the following rights and defenses in any direct action: ... (3) A defense relating to the amount of a claim or claims, filed in any action in any court or other proceeding, that exceeds the amount of this guaranty with respect to an incident or with respect to a release or threatened release, and ... (5) The claim is not one made under either of the Acts."

limit and (ii) against a claim "not one made under either [OPA or CERCLA]", but these only seem to beg the questions posed above rather than deal with them.

All of these problems could be avoided by the solution proposed by a coalition of shipowners to have the proceeds of an insurance policy (or P&I Club entry) assignable to the National Pollution Funds Center (NPFC). There is no desire on the part of Underwriters to avoid a loss under a policy, but rather to be removed from the extreme hazard of direct action. As several commenters demonstrated in the rulemaking, the Coast Guard had statutory discretion to provide that an insurance policy which included a loss-payee clause in favor of the NPFC could properly be counted as one of the assets (not necessarily the sole asset) for purposes of the vessel owner's qualification as a self-insurer. Under this arrangement, the insurer therefore would not be the "guarantor" under the Act and therefore not subject to direct action under Sec. 1016(f). That this route was not taken reflects either (1) the NPFC's own institutional reluctance to be the loss-payee and risk being second-guessed on distribution of the proceeds to claimants or (2) a conclusion by the Coast Guard that it did not have statutory authority to do so. Either way, this Subcommittee may wish to examine this alternative more closely.

Some alternative markets have suggested that they may be prepared to take the direct action exposures to which our capital is unwilling to be hazarded. An insurer has a responsibility not just to his investors, but to all policyholders, to ensure a single risk does not jeopardize the security of every other policy he issues. No sensible regulator of solvency would allow an insurer to expose his assets in this way. Perhaps these alternative markets can construct a wall of protection or asset-security that is not open to indemnity insurers. While we are sure that they have addressed all these issues, we cannot be in a position to speculate about the feasibility of their projects. We have long labored to provide the underlying protection to both the shipping and oil industries and we remain resolved to stand behind our clients for all but the most novel exposures under this new OPA regime.

In conclusion, let me add that it is disturbing to see the Interim Rule's assertion that OPA "essentially adopted the 1969 CLC's financial responsibility scheme". 59 Fed. Reg. 34211 (July 1, 1994). None of the problems identified above would arise in a foreign court under the CLC regime. Perhaps until there is a more candid recognition of the problems of the scheme that has been wrought, there will be no long-term, stable and financially solid OPA COFR market.

If the OPA rules were no less arbitrary than those enforced under the Clean Water Act and the risk of multiple limits under State legislation for a single spill were removed, then we would earnestly endeavor to continue to provide the protection to our insureds that your laws require.

Thank you.

STATEMENT OF HUGH BRYANT
ON BEHALF OF
SHORELINE MUTUAL INSURANCE
BEFORE THE
SUBCOMMITTEE ON COAST GUARD AND NAVIGATION,
COMMITTEE ON MERCHANT MARINE AND FISHERIES,
U.S. HOUSE OF REPRESENTATIVES

July 21, 1994

Mr. Chairman and members of the Subcommittee: I am Hugh Bryant, with the London law firm of Penningtons. I very much appreciate the opportunity to appear before you today on behalf of Shoreline Mutual Insurance. All of us associated with Shoreline are particularly grateful to you, Mr. Chairman, for your willingness to schedule an oversight hearing so quickly following the Coast Guard's publication of its interim rule prescribing the financial responsibility requirements that shipowners will have to meet pursuant to the Oil Pollution Act of 1990 ("OPA 90").

That legislation and the Coast Guard's rulemaking proceeding have been the subject of significant controversy during the past four years. Shoreline salutes the Coast Guard and the Department of Transportation for proceeding so openly and deliberately -- giving interested parties ample opportunity to express their suggestions and concerns -- and for publishing a rule that fully and fairly implements the financial responsibility requirements spelled out by Congress four years ago.

Shoreline has been organized expressly for the purpose of providing shipowners with liability insurance pursuant to OPA 90 and the new regulation, both of which it wholeheartedly supports. There should be no question about the availability of insurance cover for tankers under this regime. Shoreline is one source of that cover. I want to explain what Shoreline is, how its insurance will work and what it will cost, and to answer any questions the Subcommittee may have.

General Background

OPA 90 requires the operator of every ship of over 300 gross tons entering U.S. waters to provide evidence of insurance against oil and hazardous substance pollution liability to enable the Coast Guard to issue a Certificate of Financial Responsibility ("COFR").

Traditionally, shipowners have covered their oil pollution liabilities through membership in protection and indemnity ("P&I") clubs. The leading 18 clubs, comprising the International Group, today insure the liability of over 90 percent of the world's tonnage and provide insurance cover of up to $500 million per accident for oil pollution liabilities worldwide. Their insurance supported the issuance of COFRs under the Federal Water

Pollution Control Act, pursuant to which guaranteed liability limits were lower and the possibility of direct action against insurers was reserved to governmental entities.

The COFRs issued pursuant to OPA 90 will specify a maximum limit of liability for each ship based upon its gross tonnage. Those limits will be substantially higher in every case than the limits that applied before the new law was enacted. The statute permits any claimant -- including private, third-party claimants -- to sue the insurer directly, and treats the insurer as a guarantor to the full extent -- but only to the full extent -- of the applicable COFR limit.

The new law was designed to fulfil a critical public policy objective: ensuring ready access to the substantial resources that are required to pay clean-up costs and compensation in cases of oil pollution from ships. In many ways it mirrors requirements which have been adopted by 55 other countries worldwide under the International Convention on Civil Liability for Oil Pollution Damage of 1969 ("1969 CLC").

As you know, Mr. Chairman, the International Group clubs and their reinsurers have indicated, for reasons they have publicly articulated on a great many occasions, that they would not support issuance of the new COFRs required by OPA 90. The clubs have continued to provide COFR guarantees since the signing of OPA 90, with reinsurance provided mainly by Lloyd's, only because the Coast Guard has allowed ships to enter U.S. waters with COFRs based on pre-OPA 90 legislation. The new regulation makes clear that this dispensation will terminate, for tankers at least, on December 28 of this year. Very clearly, new ways to demonstrate financial responsibility will have to be found.

Shoreline: A New P&I Club

Shoreline was created as one response to that requirement. It is a new company, but it is organized along familiar lines. Shoreline, in fact, is a P&I club set up in keeping with the traditional model -- that is, as a non-profit group of shipowners banded together to indemnify each other mutually against liability resulting from the operation of their ships. It is registered and has its underwriting center in Bermuda (as do a number of the International Group clubs). Its claims processing center is based in Seattle, Washington. Its managers and directors represent many years of accumulated experience in the marine insurance community.

The terms of Shoreline's insurance are set forth in its Rules, a copy of which I am submitting for inclusion in the record (Appendix A). Those Rules are similar to the rules of the International Group clubs in all respects but one: whereas the International Group clubs cover all shipowners' liabilities in all geographic areas, Shoreline covers only pollution from oil and hazardous and noxious substances ("HNS") and only within the territorial waters and exclusive economic zone of the United States.

Shoreline will provide insurance of up to $300 million per accident against shipowners' liabilities for oil and HNS pollution in U.S. waters. The first $10 million of insurance responsibility for any one accident or occurrence will be "retained" by Shoreline, *i.e.*, paid out of its own funds without recourse to reinsurance. Shoreline will not begin writing policies, however, unless and until a full reinsurance contract covering claims in

excess of that $10 million, up to a maximum liability of $300 million, has been concluded with well-established, well-known companies. It is Shoreline's intention that the total aggregate amount of reinsurance available to it in any one policy year be in excess of $800 million.

Shoreline has already succeeded in attracting reinsurance support from some of the world's largest reinsurance companies, and is using Willis Faber & Dumas, Ltd., in London, and Willis Faber North America, Inc., in New York, as its brokers to coordinate this reinsurance. Thus, a full programme to reinsure up to $290 million in excess of Shoreline's retained $10 million responsibility in each case will shortly be put in place.

Financial Soundness of Shoreline

Shoreline must be able to respond to claims from the moment it writes its first policy. The managers of Shoreline have decided, therefore, that interim capitalization of $300 million is required -- the amount required to enable the new mutual to pay one claim to the maximum extent of the policy without recourse to reinsurance. In order to establish a fund of that size, Shoreline will shortly issue short-term bonds. The Bermuda Insurance Approvals Committee has given its approval to Shoreline conditioned on its achieving the projected funding and completing its reinsurance programme.

Beyond the proceeds of the bond issue, Shoreline's resources will be based on "calls" -- insurance premiums -- paid in by its member shipowners. Those premiums will be charged in accordance with tariffs that distinguish significantly between tankers and non-tankers.

For tankers, the tariff will be assessed on the basis of the quantity of oil the ship is capable of carrying (the deadweight tonnage of the ship) per voyage, as well as the type of oil (persistent or non-persistent) and the ship's age and construction. The Shoreline tariff will give special credit for environmentally beneficial features such as double hulls or double bottoms, thereby encouraging the deployment of such ships.

For non-tankers, which are thought to present only a very small risk of pollution, there will be an annual advance call ranging between $3000 and $5000, depending largely on the age of the ship. Premiums of this magnitude should not cause any difficulty to non-tanker owners.

Under its reinsurance contract, as I have already indicated, Shoreline would be able to recover a maximum aggregate amount in excess of $800 million from reinsurers in a given year. If the aggregate limit of reinsurance were exceeded, Shoreline would be empowered under its Rules to make "supplementary calls" on its shipowner members in order to make up any deficit. The obvious corollary to this, of course, is that surplus premiums collected in the course of a policy, according to Shoreline's Rules, may be returned to the shipowner members at the closing of that year.

This mutual supplementary call system, of course, is the same system that has supported the solvency of the International Group P&I clubs for over a century. Indeed, the

regulatory approval granted to Shoreline by the Bermuda Government is based upon the full mutuality embodied in Shoreline's Rules.

The most important point to be made about Shoreline's financial soundness, however, is that it is not, as some appear to believe, a commercial insurance company. At the risk of belaboring the point, it is a non-profit mutual -- virtually identical in structure and operation to the P&I clubs that have been the traditional providers of insurance in this market. As such, Shoreline's strength -- like that of any P&I club -- will be a function of the strength of its shipowner members. It will be the shipowner members themselves, in other words, that will represent Shoreline's real financial viability.

The Cost of Shoreline's Insurance

Concern has been voiced about the cost of Shoreline's insurance to its shipowner members. There can be no question that the cost will be higher than the cost of cover traditionally available from the International Group clubs. It should be no surprise, after all, that OPA 90's requirement that insurers guarantee the availability of more adequate resources to deal with the financial consequences of oil pollution carries with it a somewhat higher price tag to shipowners than the far less satisfactory regime that Congress voted to replace.

But it is important that the cost of Shoreline's insurance not be exaggerated. Remember that, for tankers, Shoreline's tariff is designed to facilitate the attribution of incremental insurance costs to specific voyages and cargoes, enabling shipowners to pass such costs through to charterers, to cargo owners, and ultimately to the consumer of refined oil products. The attractiveness of this feature is that the increase in insurance costs resulting from the establishment of the higher levels of financial responsibility required by OPA 90 can be distributed as widely and thinly as possible to a very large class of ultimate beneficiaries: the public.

The Coast Guard's final Regulatory Impact Analysis ("RIA") issued in connection with the new regulation makes clear, in fact, that the increase in the cost of gasoline at the pump will be almost negligible. The RIA offers a projection of insurance costs under OPA 90, using as a baseline the P&I clubs' OPA 90 surcharge. The Coast Guard assumed that the premiums assessed by Shoreline and First Line (another facility established to provide OPA 90 insurance) would not exceed seven times that surcharge (29 cents per grt per voyage). The RIA calls this assumption an "overly cautious estimate of insurance guarantee costs, so as not to under-inflate the possible costs."[1/]

Even with an estimate as conservative as that, the RIA predicts that the additional cost of a barrel of imported crude oil or refined product, such as gasoline, would be less than $0.145. The potential increase in the cost of a gallon of refined product would be $0.00345 -- less than two-fifths of a cent per gallon at the pump.[2/]

[1/]United States Coast Guard, *Regulatory Impact Analysis - Financial Responsibility for Water Pollution (Vessels)* [CGD 91-005], June 1994, p. 81, n. 98.

[2/]*Id.*, p. 81.

That is good news, to be sure. But the real story is likely to be even more encouraging. While the numbers in Shoreline's proposed tariff (Appendix B) cannot be treated as final until reinsurance arrangements are fully in place, Shoreline fully anticipates that its premiums will be lower than those assumed for purposes of the Coast Guard's analysis. The actual impact at the pump, therefore, is likely to be even smaller than the tiny increment projected in the RIA.

Moreover, the RIA points out another way in which its estimates can be said to be overly cautious. It notes that, because Shoreline and First Line will be absorbing the greatest OPA 90 risks, P&I club payouts are likely to decrease substantially. That reduction may have the effect of reducing the P&I clubs' reinsurance premium, "ultimately offsetting the cost to vessel operators of First Line and Shoreline COFR insurance."[3/]

In sum, there should be no concern whatsoever on the part of Congress about whether the market can afford the cost of Shoreline's insurance.

Guarantees, Direct Action, State Law, and Unlimited Liability

Before closing, I want to add just a few words about features of OPA 90 and the Coast Guard's regulation that have been the subject of the greatest controversy and, I believe, the greatest misunderstanding. I am referring to the guarantor and direct action provisions of OPA 90, to the continued availability to claimants of state law remedies, and to the possibility that the new regime will expose guarantors to unlimited liability.

First, the guarantor and direct action concepts were not introduced into U.S. law by OPA 90. They were included in the Federal Water Pollution Control Act of 1970, and reflected similar provisions of the 1969 Civil Liability Convention.

It is true that, under OPA 90, direct action will be available to private party claimants, whereas only the Federal Government could avail itself of direct action under the Federal Water Pollution Control Act. But that is only because the earlier legislation did not go as far as the 1969 CLC in that respect. The Convention does enable private claimants to pursue direct action against insurers.

Similarly, state law has never been pre-empted by federal water pollution legislation in the U.S. Thus, there is nothing new in OPA 90 about the possibility of claims being brought under state law.

Finally, there is simply no basis for believing that a guarantor might somehow find itself subject to claims that exceed the limit of its guarantee. OPA 90 could not be clearer on this point. Section 1016(g) says, quite simply:

> Nothing in this Act shall impose liability with respect to an incident on any guarantor for damages or removal costs which exceed, in the aggregate, the amount of financial responsibility

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[3/] *Id.*, p. 82, n. 101.

required under this Act which that guarantor has provided for a responsible party.

While OPA 90 makes it easier to break a shipowner's liability limit than was the case under prior law and under the 1969 CLC, it does not create any possibility of breaking the limit applicable to the guarantor. The Coast Guard emphasized this point in issuing the interim final rule on COFRs, and even created some additional comfort for guarantors in the forms appended to the rule.

I am aware that an argument can be made under U.S. law that the limits of a policy do not apply in a case in which a claimant proves bad faith on the part of an insurer. Such claims have been possible under existing law, however, and so, again, they represent nothing new.

Shoreline does not find anything in OPA 90 or the new regulation, in short, that will prevent it from providing the kind and quality of insurance necessary to support the issuance of new COFRs by the Coast Guard. It is true that OPA 90 represented a dramatic and innovative step forward in environmental protection legislation; it may well require the industry to formulate a comparably innovative response. We think Shoreline represents one important way in which the shipowner community can address its obligations under this important new law, and without incurring any undue burden. We fully anticipate that there will be others as well.

Conclusion

The Coast Guard has given the Shoreline concept an "in principle" approval in a letter from Mr. Daniel Sheehan, the Director of the National Funds Pollution Center, dated December 1, 1993. (Appendix C.) Similarly, the Bermuda Registrar of Companies, in a letter dated July 19, 1994, has indicated that "Shoreline has been approved as an insurer for the purpose of the Bermuda Insurance Act 1978 subject to the completion of its reinsurance protections and a bond offering." (Appendix D.) Still, Shoreline is not yet authorized to start writing insurance. That is because the final approvals from the governing authorities will be given only when Shoreline has its final arrangements in place.

As you know, Mr. Chairman, the principal impediment to the completion of those arrangements, until very recently, was the lack of a COFR rule. Now that the Coast Guard's interim final regulation is available and obligations are clear, however, definite commitments can be made; Shoreline, therefore, will be able to complete its remaining arrangements in short order. But the key to Shoreline's success -- indeed, to the success of all schemes for the establishment of appropriate levels of financial responsibility by shipowners -- is that the maritime community and its insurers be left in no doubt that OPA 90 and the new COFR rule mean what they say, and that the deadlines established in the rule will be strictly enforced.

On the other hand, if the wisdom and workability of OPA 90 are seriously called into question at this late date -- notwithstanding the thoroughgoing analyses that have already been undertaken by Congress and the Executive Branch -- shipowners, reinsurers, and potential investors are likely to find themselves plunged back into the uncertainty that

preceded the Coast Guard's publication of the new regulation on July 1. I cannot emphasize strongly enough how damaging such uncertainty would be. It is not too much to suggest that official expressions of doubt about the effectiveness of OPA 90 at this stage might well become self-fulfilling prophesies.

What is critically needed now, Mr. Chairman, is a period of calm and stability. Allow the shipowner and insurance communities to digest the implications of the new regulation and to put appropriate arrangements in place. Only then will the requirements established by Congress finally be met. Shoreline looks forward to moving past this four-year-long debate and into full-scale implementation of OPA 90 at long last.

Thank you, Mr. Chairman, for the opportunity to present this statement. I look forward to any questions that you or other members of the Subcommittee may have.

Attachments (Appendices A-D)

APPENDIX A

SHORELINE MUTUAL INSURANCE 1994 RULE BOOK

SHORELINE
MUTUAL INSURANCE 1994 RULE BOOK

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Shoreline - the alternative view

Since the introduction of the Oil Pollution Act 1990, we have witnessed a period of tremendous uncertainty in the shipping industry. Uncertainty has produced hostility, and dialogue between shipowners, through their P & I Clubs, and the United States Coast Guard has been cold.

A positive response was required and Shoreline Mutual has been established to provide this response.

Operating alongside the P & I Clubs, Shoreline Mutual provides cover up to US$300 million any one accident, and provides the guarantee for the Certificate of Financial Responsibility required under Section 1016 of OPA.

Shipowners worldwide are faced with ever mounting costs in an environment which is imposing increasingly heavy burdens. Shoreline aims to ensure that the cost of this particular liability is passed on so that the burden is shared, ultimately with the public whom OPA 90 was established to protect, thereby minimising the impact for everyone.

Shoreline Mutual has been established as the alternative approach to OPA 90. We believe that Shoreline Mutual will become the essential approach.

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Shoreline Addresses

Club Address:

Shoreline Mutual (Bermuda) Limited
44 Church Street
PO Box HM2064
Hamilton HM HX
Bermuda

Tel: (809) 295-5688
Fax: (809) 292-1867

Bermuda Managers' Address:

Shoreline Mutual Management (Bermuda) Limited

Address details as above

Managers' London Agents:

Shoreline Mutual Management Limited
PO Box 201
Esher
Surrey
KT10 8YJ

Tel: 071-606 1247
Fax: 071-606 1248

Managers' USA Agents:

Shoreline Mutual Management Services
PO Box 99288
Seattle
Washington 98199
USA

Tel: (206) 282-7324
Fax: (206) 542-0173

APPENDIX A-3

SHORELINE MUTUAL (BERMUDA) LTD RULES

1 *Memorandum and Bye-laws*

These rules are subject to the Memorandum and Bye-laws of Shoreline Mutual (Bermuda) Limited, a company registered in Bermuda. Copies of the Memorandum and Bye-laws are available on request from the managers.

2 *Class of Cover Offered by the Association*

The Association offers Protection and Indemnity (P & I) cover for

(a) actual or threatened discharges of oil from an entered ship into or upon navigable waters, adjoining shorelines or within the exclusive economic zone of the United States of America as defined in the US Oil Pollution Act of 1990 and in any legislation of a State of the United States of America to the same effect and

(b) release or threatened release of a hazardous substance from an entered ship into the environment as defined in the US Comprehensive Environmental Response Compensation and Liability Act of 1980.

Rule 19 lists the liabilities covered. Where there is a conflict between rule 19 and the other rules, rule 19 shall override any other express or implied terms of the other rules.

3 *Definitions*

In these rules the following definitions are intended.

"The Association".
Shoreline Mutual (Bermuda) Limited.

"Associated Company".
in relation to any member, a holding company, wholly owned subsidiary company, or fellow wholly owned subsidiary of the same holding company.

"Directors",
a quorum of the directors of the Association meeting as directors.

"Dollars" or "$",
United States dollars.

"Entered Ship",
a ship entered in the Association and one in respect of which evidence of financial responsibility is required pursuant to section 1016 of the US Oil Pollution Act of 1990.

"Evidence of Financial Responsibility",
evidence of financial responsibility for oil pollution as defined further in rule 19.

"Fleet Entry",
the entry of more than one ship by one or more members on the basis that those ships will be treated together as a fleet for underwriting purposes.

"Hazardous Substance",
such substances as are defined in section 101 of the US Comprehensive Environmental Response Compensation and Liability Act of 1980

"Hull Policy",
an insurance policy covering loss or damage to the hull and machinery of a ship, including any excess liability policy.

"Managers",
Shoreline Mutual Management (Bermuda) Limited.

"Member",
any owner of an entered ship, or co-assured member as defined in rule 9.

"Oil",
such oil as is defined in section 1001 of the US Oil Pollution Act of 1990 or in the legislation of any State of the United States of America and other territories, as defined in section 1001 (36) of the Oil Pollution Act of 1990, to the same effect.

"Owner",
an owner, part owner, charterer, mortgagee, trustee, operator, manager, or builder of a ship or an associated company of any of these.

"Policy Year",
a year from noon UTC on the date specified by the directors from time to time as the commencement of the policy year.

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"Protection and Indemnity" or "P & I".
insurance against shipowners' liabilities to third parties as defined in the rules of a P & I association.

"Rules".
the rules of the Association.

"Ship".
a ship, boat, hovercraft, jetfoil or other vessel capable of navigation in or on water for any purpose, but excluding a fixed platform, fixed rig, or remotely operated vehicle.

"Terms of Entry".
in relation to any entered ship, the name, size in gross and deadweight tons of the ship, the risks covered by the Association, and the rate of contribution.

In interpreting these rules, words denoting the singular shall denote also the plural and vice versa; the masculine gender shall include the feminine and vice versa, and any reference to persons shall extend also to partnerships and companies.

Any notes to the rules (in italics) are not part of the rules but are merely included for explanation purposes.

4 *Application for Entry*

An owner may apply for entry of a ship or ships in the Association using an application form obtained from Shoreline Mutual Management Ltd, Shoreline Mutual Management Services or a broker. The details given by the owner on the application form will, if the entry is accepted, form the basis of the contract of insurance between the owner and the Association, which contract is founded upon the utmost good faith. Thus, if the owner supplies false details of any kind or omits to disclose material details in the application form, the managers may terminate the entry from its inception without notice. Once his entry is accepted, the member undertakes to inform the managers promptly about any changes in the details originally recorded on the application form and about any material details which have arisen after his entry was accepted.

For the avoidance of doubt the terms in this rule apply equally to co-assured members (see rule 9).

5 *Membership*

(a) Any owner who enters a ship in the Association becomes a member of the Association from the date on which the entry is accepted by the managers for an initial period to expire twelve months from the inception date to be determined by the directors and subsequently for a single policy year.

(b) A member does not acquire a share or interest in the funds of the Association by virtue of his membership.

(c) An owner will no longer be a member when for any reason he ceases to have any ships entered in the Association. However, until and unless a release is agreed by the managers in accordance with rule 21, a former member remains bound by all the obligations contained in these rules, including the obligation to pay supplementary calls.

(d) Applications for insurance may be made and accepted in respect of ships with different beneficial ownerships on terms that the ships concerned shall be deemed (for these insurance purposes only) to form part of the specified fleet whereby the Association shall deal with the entries of such ships in combination and not individually, in consideration for which all members within each such fleet entry shall accept joint and several liability to pay all amounts due to the Association by way of calls or otherwise in respect of all ships within that fleet entry. Such joint and several liability shall continue after cessation of entry in respect of amounts due to the Association.

6 *Acceptance of Entries*

The managers have discretion to accept or reject any application for entry, even from an existing member, without giving reasons. The managers have no discretion to accept any entry where any amount due in accordance with rule 20 has not been paid.

7 *Certificate of Entry*

As soon as possible after a ship has been entered, the managers will issue to the member a certificate of entry which will show:

(i) the names of the owner and any co-assured members;

(ii) the names of any mortgagees and the text of any agreement with them (see rule 10);

(iii) the name, size in gross and deadweight tons of the ship;

(iv) the risks covered;

(v) the date when the entry began;

(vi) any other terms of entry agreed.

These details will be entered in the Association's computer data bank. The member consents to such electronic storage of information, and the managers are authorised at any reasonable time to provide a member with a copy of the data entries about him on request. A member will not be entitled to see data kept about any other member.

8 *Continuation of Cover and Changes in the Terms of Entry*

A member will remain a member for the initial single policy year and subsequently for each succeeding policy year, in each case subject to the original rates and terms of entry agreed when the ship was first entered or any subsequent agreed variations thereof unless the entry is terminated in accordance with the provisions of rule 30. Provided always that the Association may at any time give notice to members of changes in rates or terms of entry, which changes shall, in default of agreement by the member concerned, take effect at the beginning of the policy year immediately following the policy year during which such notice shall have been given.

9 *Co-assured Members*

(a) A ship may be entered in the Association by her owners, charterers or any others defined as "owners" in rule 3. Any associated companies of the members concerned in the entry (see rule 3) can, by their being named as co-assured in the certificate of entry, benefit from the entry, subject to the provisions of these rules, in particular rule 4.

(b) The rights and obligations of those named as co-assured towards the Association are as follows:

(i) where the registered owner and the co-assured (not being the registered owner of the ship) share the functions and duties of a shipowner under a contract, the co-assured's cover in the Association extends only so far as that of the registered owner;

(ii) there will be no recovery by one co-assured where the claim has already been reimbursed to another co-assured;

(iii) those named as co-assured are jointly and severally liable to pay calls for contribution to the Association;

(iv) receipt by any of those named as co-assured of a payment will be equally sufficient to discharge the Association from any obligations in respect of that payment; and

(v) notice to any of those named as co-assured will be taken as notice to all those concerned in the entry; and the knowledge of any one of those named as co-assured will be taken to be knowledge shared by them all.

10 *Mortgagees*

Where an entered ship is mortgaged, it is a condition of membership that the member consents to the interest of the mortgagees being noted on the certificate of entry. The member also agrees to allow the managers, subject to the provisions against assignment in rule 31 and for automatic cancellation of cover in rule 30, to give undertakings to the mortgagees:

(i) upon notice to the managers by the mortgagees that the member is in default under the mortgage to pay the mortgagees whatever would otherwise have been paid by the Association to the member;

(ii) to inform the mortgagees if the member gives notice of his intention to withdraw the mortgaged ship from the Association;

(iii) to give not less than five working days' notice to the mortgagees if the managers intend to cancel the member's entry of the mortgaged ship, except if the entry terminates automatically under rule 30, in which case notice will be given to the mortgagees as soon as practicable thereafter.

11 *Right to Insurance*

(a) A member in any particular policy year is entitled to recover from the Association subject to these rules and the terms of entry any payments which he has made in respect of the legal liabilities listed in rule 19 which result from incidents occurring during that policy year (or, where the member's entry has been accepted after the inception of that policy year, which result from incidents occurring after the time of entry during that policy year) and out of the ownership or management of an entered ship. As between the member and the Association, liabilities which arise in any other manner are not covered.

(b) Unless the directors otherwise agree, a member cannot recover from the Association any payment in respect of a claim covered under these rules and the terms of entry of the ship concerned, unless the member has first made a complete payment to the claimant and obtained a receipt and release from further liability or other proof of payment acceptable to the managers. The only exception to rule 11(b) is in the case of legal or other fees for the services of lawyers or experts, covered under rule 19.2 where, provided that the managers have made the appointment or approved the appointment, the lawyer or expert will be paid direct by the Association. The managers will inform the member when fees have been paid and any amount paid will appear on the member's claims record (see also rule 19.2).

(c) In the event that the member recovers from the Association and the Association makes a direct payment pursuant to a Certificate of Financial Responsibility (see rule 19) the member will reimburse the Association such sum, if any, by which the aggregate of the sum recovered by the member and the direct payment pursuant to the said certificate exceeds $300,000,000. In the event of there being such an excess the member will hold on trust for the Association such part of the sum he has recovered from the Association as is equal to the excess.

12 *Hull and War Risks Policies*

Every ship entered in the Association will be deemed to be insured (by insurers other than the Association) against war, hull and machinery risks for a value not less than her current sound market value in charter-free condition. The terms of her hull policy will be deemed to be not less wide than those of Lloyd's Marine Policy MAR form 1.10.83 with Institute Time Clauses (Hulls) 1.10.83 attached, and she will be deemed to be insured up to her current sound value against war risks. Any claim which could be recovered from such policies or any other insurance policies will not be recoverable from the Association.

13 P and I Cover

Every ship entered in the Association will be deemed to be entered in a Protection and Indemnity Club on terms of entry deemed to be not less wide than those of the United Kingdom Mutual Steamship Association (Bermuda) Limited current at the date when entry is accepted or such other terms as the managers may determine. Any claim which could be recovered from such entry or any other entry will not be recoverable from the Association, except where such a claim arises as a result of a liability as defined in rule 19.1.

14 Limitation of Cover

(a) In no circumstances will the Association be liable, either to a member or otherwise for any amount in excess of a member's legal liability in respect of a given accident or occurrence, or in excess of the limitation amount specified for the entered ship under the US Oil Pollution Act s.1004 (a) and (d) or under the legislation of a State of the United States of America (whether or not the member is in fact able to limit his liability to that amount).

Provided always that the limit of cover provided for each accident or occurrence is $300 million (300,000,000 US dollars).

(b) If a member, by virtue of his not being a shipowner, is not entitled to any limitation of liability which he could have enjoyed if he were a shipowner, any reimbursement by the Association is limited to the amount to which a shipowner could have limited his liability, as assessed by the directors, or $300 million, whichever is the greater.

Note - This clause is intended to refer in particular to associated companies of members, named as co-assured, who are not entitled to limitation of liability as shipowners. An example would be a member's subsidiary company which provided crew management on an entered ship

15 Notice of Claim

(a) Every incident likely to give rise to a claim under these rules and every claim made against a member in respect of such incident shall be notified to the managers as soon as possible but in no case later than 6 months after the incident or, as appropriate, after the member has received

notice that the claim is being or may be made against him. In each case all relevant documents and information shall be given to the managers.

(b) If notice is not given in accordance with (a) above the member will not be entitled to recover from the Association in respect of the incident or claim in respect of which proper notice was not given (unless and to the extent that the directors in their discretion decide otherwise) and the member will be obliged to indemnify the Association in respect of any direct payment or part thereof made pursuant to any Certificate of Financial Responsibility as a result of the failure to give proper notice.

(c) No liability should be admitted or payment made in respect of a claim in which reimbursement from the Association will be sought until and unless the managers have given their approval. If no prior approval has been obtained from the managers, there will be no reimbursement by the Association without the directors' approval and the member will be obliged to indemnify the Association in respect of any direct payment or part thereof made pursuant to a Certificate of Financial Responsibility as a result of the failure to obtain prior approval.

16 *Duty to Act as a Prudent Uninsured*

(a) In dealing with liabilities potentially covered by the Association, a member must act as prudently to protect his interests as he should have done if not insured against the risk in question by the Association.

(b) If the member fails to act as a prudent uninsured the member will not be entitled to recover from the Association in respect of the incident or claim in respect of which he fails so to act (unless and to the extent that the directors in their discretion decide otherwise) and the member will be obliged to indemnify the Association in respect of any direct payment or part thereof made pursuant to a Certificate of Financial Responsibility as a result of such failure.

17 *Classification and Maintenance*

(a) Subject to rule 19.1(b) and, unless otherwise agreed in writing between the member and the managers, the following conditions are terms of the insurance of every entered ship:

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(i) The ship must be and remain throughout the period of entry classed with a Classification Society approved by the managers.

(ii) Any incident or condition in respect of which that Classification Society might make recommendations as to repairs or other actions to be taken by the member must be promptly reported to that Classification Society.

(iii) The member must comply at all times with all the rules, recommendations and requirements of the Classification Society relating to the entered ship and where that Classification Society specifies a time or times within which action must be taken in relation to the entered ship the member must take such action within such time or times.

(iv) The member authorises the managers to inspect any records or documents and obtain any information relating to the maintenance of class of the entered ship in the possession of any Classification Society with which the ship is or at any time has been classed, and will where necessary authorise such Classification Society or Societies to disclose and make available such documents and information to the managers upon request by the managers and for whatsoever purposes the managers may consider necessary.

(v) The member must immediately inform the managers if, at any time during the period of entry, the Classification Society with which the ship is classed is changed and advise the managers of all outstanding recommendations, requirements or restrictions specified by any Classification Society relating to that ship as at the date of such change.

(vi) The member must comply with all statutory requirements of the country of the ship's flag relating to the construction, adaption, condition, fitment and equipment of the entered ship and must at all times maintain the validity of such statutory certificates as are issued by or on behalf of the state of the ship's flag in relation to such requirements.

Unless and to the extent that the directors otherwise decide, the member shall not be entitled to any recovery from the Association in respect of any claim arising during a period in which the member is not fulfilling or has not fulfilled his obligations under this rule.

(b) (i) The managers may as a condition of entry or re-entry of a ship in the Association require the member or prospective member to submit the ship to survey by a surveyor appointed by the managers. The managers in their discretion may require the member or prospective member to bear the expense of such a survey.

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In the light of such survey the managers may:

(a) refuse the entry or re-entry of the ship; or

(b) refuse the entry or re-entry of the ship until repairs or other action recommended by the surveyor have been carried out to the satisfaction of the managers within any time limit prescribed by the managers; or

(c) accept the entry or re-entry of the ship on such special terms as the managers may in their discretion decide.

(ii) Without prejudice to any warranties or other duties and obligations imposed on a member under these rules or general law, the managers may at any time and from time to time require a member to submit his entered ship to survey by a surveyor appointed by the managers on a date and at a place agreed between the member and the managers and within such time limit as may be specified by the managers. The managers may in their discretion require the member to bear the expense of such a survey or they may treat it as an expense payable by the Association at their discretion.

In the light of such survey or in the event of failure by the member to submit the entered ship to such survey within the time limit specified by the managers, the managers shall have the power, in their discretion, to:

(a) terminate the entry of the ship forthwith; or

(b) amend, vary or impose special terms on the terms of entry of the ship with immediate effect in such manner as they think fit for such time or period as they may specify.

(iii) Any recommendations or observations of a surveyor acting under any part of this rule shall be treated as within the actual knowledge of the member. Any failure by the member to implement the said recommendations shall entitle the directors in their discretion to refuse, in whole or in part, a claim for recovery from the Association in respect of any incident whatsoever occurring after such recommendations have been made.

(e) The member will indemnify the Association in respect of any direct payment or part thereof made pursuant to a Certificate of Financial Responsibility as a result of any failure to comply with the terms of this rule.

18 *Privity*

(a) The provisions of the English Marine Insurance Act 1906 are specifically incorporated in these rules. Members are reminded in particular that Section 39(5) of the Marine Insurance Act provides.

"In a time policy there is no implied warranty that the ship shall be seaworthy at any stage of the adventure, but where, with the privity of the assured, the ship is sent to sea in an unseaworthy state, the insurer is not liable for any loss attributable to unseaworthiness."

(b) If an entered ship is sent to sea in an unseaworthy state with the privity of the member the member will be obliged to indemnify the Association in respect of any direct payment or part thereof made pursuant to a Certificate of Financial Responsibility as a result of that unseaworthiness.

19 *Evidence of Financial Responsibility*

The Association will provide to the US Coast Guard for each entered ship evidence of insurance coverage on behalf of:

(a) the operator of the ship as defined in section 1001 (26) of the Oil Pollution Act of 1990 (OPA) against the liabilities defined in section 1002 of OPA up to a maximum limit of liability in accordance with section 1004 of OPA, confirming that the Association consents to be sued directly in respect of such liabilities, subject to the provisions of OPA, and in particular section 1016, in order to enable the United States Coast Guard to issue a Certificate of Financial Responsibility (COFR) in accordance with Section 1016 of the US Oil Pollution Act of 1990 showing evidence of liability coverage up to the limits provided by section 1004 of the Act of 1990 and

(b) the owner and operator of the ship as defined in section 101 (20) of the Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA) against the liabilities defined in section 107 of CERCLA up to a maximum limit of liability in accordance with section 107 of CERCLA, confirming that the Association consents to be sued directly in respect of such liabilities, subject to the provisions of CERCLA, and in particular section 108, in order to enable the President to furnish a Certificate of Financial Responsibility in accordance with section 108 of CERCLA, showing evidence of liability coverage up to the limits provided by section 107 of CERCLA

but in no event shall the limit of cover for each incident exceed $300 million (300,000,000 US dollars).

19.1 *Liability for actual or threatened discharge of oil or release of a hazardous substance*

(a) A member is covered by the Association for any liability as defined below in respect of

(i) an actual or threatened discharge of oil from an entered ship into or upon navigable waters adjoining shorelines or within the exclusive economic zone of the United States as defined in the US Oil Pollution Act of 1990 or in the legislation of any State of the United States of America to the same effect and

(ii) a release or threatened release of a hazardous substance from an entered ship into the environment as defined in the US Comprehensive Environmental Response Compensation and Liability Act of 1980

but only up to a maximum of $300 million (and subject to the provisions of rule 14) for any one incident.

(b) The following are defined as liabilities and are covered:

(i) liability for removal costs and damages pursuant to the US Oil Pollution Act of 1990 or any legislation of a State of the United States of America to the same effect;

(ii) liability to pay fines or penalties pursuant to the US Oil Pollution Act of 1990 or any legislation of a State of the United States of America to the same effect;

(iii) liability for costs of removal and remedial action and other necessary costs of response and damages pursuant to the US Comprehensive Environmental Response Compensation and Liability Act of 1980;

(iv) liability to pay fines or penalties pursuant to the US Comprehensive Environmental Response Compensation and Liability Act of 1980.

Provided always that it is a condition precedent of cover in respect of such liabilities that the member

(aa) undertakes to make quarterly declarations in arrears, at the latest within two months of each quarter ending 20th May, 20th August, 20th November and 20th February, of all voyages carrying cargo to or from ports or places to which OPA 90 or CERCLA 80 applies, giving the date of such voyages, the nature of the cargoes carried (persistent oil or other cargo) and the name of such United States port or place at which the cargo was first loaded or discharged;

(bb) complies with the said undertaking. If the Association becomes liable under a Certificate of Financial Responsibility to pay any amount while a member is in breach of this proviso, the Association shall have liberty to recover the amount so paid from the member; and

(cc) agrees that the managers may at any time, upon giving reasonable notice, inspect the member's voyage or other records to verify the declarations made under (aa) above; the member consents to such inspections and their cost shall be borne by the member.

19.2 *Experts and Lawyers*

(a) A member is covered by the Association in respect of fees and disbursements of experts, surveyors and lawyers instructed by the managers or by him with the managers' approval to investigate, advise upon and defend claims covered under these rules.

(b) If a member wishes to instruct an expert, surveyor or lawyer, he must obtain the approval of the managers, or else the fees of the firm appointed will not be paid by the Association.

(c) Where an expert, surveyor or lawyer has been instructed the member agrees that such expert, surveyor or lawyer will be paid by the Association direct. The managers will inform the member concerning the fee to be paid and the payment will be recorded in the member's claims record. If a member advises the managers that he considers that a particular fee or expense is unreasonable, the managers will investigate and use their best endeavours to ensure that only a reasonable amount is charged.

20 *Members' Contributions to the Association's Funds*

(a) A member's liability to contribute to the funds of the Association is unlimited. The purposes for which contributions may be called by the directors and collected by the managers are:

(i) to reimburse to members claims settled or expected to be settled under rules 19, 19.1, or any other terms of entry allowing payment to the member;

(ii) to make direct payments pursuant to Certificates of Financial Responsibility.

(iii) to pay whatever reinsurance premiums may be considered necessary by the directors;

(iv) to pay fees and expenses to lawyers, correspondents and experts and brokerage to brokers;

(v) to pay to the managers whatever amounts may be agreed by the directors for the purposes of administration of the Association;

(vi) to provide funds to establish solvency margins or guarantee funds if required by law to permit the continued operation of the Association;

(vii) to establish contingency reserves if approved by the directors;

(viii) to make up any deficit in the funds of the Association;

(ix) for any other purpose agreed by the directors.

(b) (i) The amount of a member's contribution, that is his rating, will be assessed and agreed with the member by the managers, who will take into consideration the type of the member's ship, the member's claims record and future exposure to liability claims, and his fair share of the items listed under rule 20(a)(iii) to (ix).

(ii) A member's rating will be expressed as a US dollar or other agreed currency amount to make an estimated total cost.

(iii) The estimated total cost will be paid by the member as an advance call. The amount of the advance call is determined by the managers at the start of the entry or of the policy year but the supplementary call or calls, expressed as a percentage of the advance call, are determined by the directors at any time thereafter until the year is closed under rule 22.

(iv) Advance calls are payable in the policy year and supplementary calls are payable as determined by the directors.

(c) (i) Advance calls shall be paid according to the number of voyages during which the entered ship is expected to be within United States waters as defined in Rule 19.1.(a), provided always that a minimum of 65 days' advance calls, as assessed by the managers, is paid in addition to the calls paid for the period of anticipated trading, so that, at any time during the currency of a ship's entry, 65 days' advance calls shall have been paid in addition to any call paid in respect of a period during which the ship is trading in United States waters.

APPENDIX A-18

(ii) Any other amounts payable to the Association except release calls by or on behalf of a member must be paid within 60 days of the issue of a debit note by the managers failing which such amounts shall incur interest at 5% above the London Interbank US Dollar Six Month Offer Rate (LIBOR) calculated from the latest payment date specified in the debit note until the actual payment date. The interest rate will be fixed on the first working day of each month during the period when the amount in question remains unpaid.

(iii) Where such an amount remains unpaid for more than 90 days after the issue of the debit note then, unless otherwise agreed with the managers, cover will automatically lapse (see rule 30).

(iv) No claim of any kind by a member against the Association will be allowed as a set-off against liability to pay in full calls or other amounts debited by the Association.

(v) If a member defaults in payment of calls or any other amounts due to the Association, and the directors agree that these amounts are unrecoverable, then the other members shall make good the deficit.

21 *Release Calls*

(a) A member or former member is always liable to pay calls for contribution to the Association and cannot be released from such liability without the written agreement of the managers. If at the time a member seeks to be released, the association has issued debt in the form of bonds or other instruments of indebtedness, the managers have no power to release members or former members from their obligations under rule 20, so long as the debt remains unsettled by the Association in respect of principal or interest.

(b) Following termination of a member's cover the managers may but are not obliged to assess a release call based on an estimate of the member's liability to pay future supplementary calls. On receipt of such assessment the former member must within 30 days thereafter (which period can be extended by the managers on such terms as they in their sole discretion think fit):

either

(i) pay the release call, in which case the former member will be discharged from further liability to the Association for future supplementary calls:

or

(ii) elect to pay future supplementary calls (whether less than, more than, or the same amount as the assessed release call) as and when they become payable and to secure such payment by means of a bank guarantee. Such supplementary calls are payable in the manner and on the terms specified in rule 20(c) and the former member is discharged from liability for supplementary calls only when all such supplementary calls and any interest due thereon have been paid in full. The managers have discretion to reject the guarantee if its wording or the bank providing the security are not acceptable to them. Should no guarantee be offered or should the managers reject the guarantee, then the release call assessed by the managers must be paid either within 30 days of receipt by the former member of the assessment by the former member or forthwith if more than 30 days has expired prior to rejection of the guarantee. If such payment is not made, then the former member also remains liable under rule 21(a) to pay any sums in excess of the release call which may be assessed by way of future supplementary calls.

22 *Closing a Policy Year*

(a) The directors may at any time after the end of a policy year declare that the year is closed. This means that the members entered during that policy year are released from liability to pay further supplementary calls in relation to that year.

(b) Before closing a policy year directors may:

(i) make supplementary calls;

(ii) return any surplus to the members in proportion to the amount of their contributions, except where a member has paid a release or has been expelled from the Association for non-payment of contributions, in which cases returns will not be given to the members concerned.

(c) Before or after closing a policy year the directors may:

(i) transfer amounts which they judge to be surplus to the requirements listed in rule 20(a) to reserves or to the credit of any other policy year;

(ii) transfer amounts from any other policy year to make up a deficit.

23 General Powers of the Directors Concerning Calls

The directors have power to decide:

(i) for the purpose of calculating whether supplementary calls are due in respect of a policy year, or for any other purpose, what claims or expenses will be considered to have arisen during that policy year;

(ii) who are the members liable to pay such a supplementary call or to pay any other amounts required by the Association;

(iii) the amount payable in respect of such a call by each member.

24 Set-off by the Association

If any amount is owed by a member to the Association, the managers will be entitled to deduct that amount from any payment due to the member.

25 Off Risk

Provided that the member gives at least 65 days' notice beforehand to the managers, a member may take an entered ship off risk in respect of the liabilities covered by the Association, for a specified period, by agreement. The managers will allow an appropriate return of call in their discretion.

26 Security for Calls

The managers may at any time require as a condition of entry or continued entry of a ship that a member shall provide security for the payment of calls or other amounts due to the Association in the form of a bank guarantee for an amount specified by the managers given by a bank approved by the managers. If a member fails to arrange such a bank guarantee within 15 days of being called upon by the managers to do so, the entry of the ship concerned will automatically cease without further notice.

The Association shall have a lien including a right of arrest on the ships of a member (including those of a co-assured) for amounts owed to the Association by the member.

27 *Reinsurance*

The directors may reinsure any of the liabilities covered by the Association with any reinsurer on such terms and rates as they consider appropriate.

28 *Investment*

(a) The funds of the Association may be invested by the directors by means of the purchase of such stocks, shares, bonds, debentures or other securities or the purchase of such currencies, commodities or other real or personal property, or by means of being deposited in such accounts as they think fit, or by such other method as they may approve.

(b) Unless the directors otherwise decide, the funds of all policy years and of any reserve account standing to the credit of the Association shall be pooled and invested as one fund.

(c) When funds are so pooled the net investment income arising thereon including any realised capital gains or losses shall, unless the directors otherwise decide, be credited or debited as the case may be to the policy year in which such income, gains or losses arise.

29 *Decisions and Powers of the Directors*

(a) Where the approval or other decision of the directors is required in accordance with these rules, it can be given at a meeting of the directors of the Association.

(b) Even in those circumstances in which the member would not otherwise be able to obtain payment of a claim under the rules the directors may in their discretion pay a claim in full or in part and on such terms as they think fit.

(c) Nothing done or not done by the directors or managers on any particular occasion in relation to any matter whatsoever shall be treated as an admission or promise that the Association will not rely strictly on its rights under the rules in relation to that particular matter or any other or as a waiver of such rights.

30 *Termination of Cover*

(a) In the following circumstances all the entries of ships by a member will be terminated:

(i) if the member owns or operates the entered ships as an individual (that is not through a company), his entries will be cancelled if he becomes bankrupt or makes any arrangement or composition with his creditors as an alternative to bankruptcy or has been certified as insane or has died;

(ii) if the member is a company, its entries will be cancelled if a winding-up order is made, or if a receiver or administrator is appointed, or if any of its property is seized by a creditor except where an entered ship is arrested as part of a claim covered under these rules, or the rules of the P & I association in which the ship is entered. Where the managers are satisfied that a winding-up order or receivership, or any other liquidation, is part of an amalgamation or reconstruction, and that the position of the rest of the membership is not prejudiced, they may agree that the member's entries will continue despite the winding-up;

(iii) if in accordance with rule 26 a member has been requested to provide security for calls, and no security acceptable to the managers has been provided within 15 days;

(iv) if a member fails to settle a debit note from the Association within 90 days, in accordance with rule 20 (c) (iii).

(b) In the following circumstances the entry of a particular entered ship will be terminated:

(i) if the member ceases to be the owner of an entered ship (as defined in rule 3), or ceases to have the interest in her specified in the certificate of entry (for example as crew manager);

(ii) if the entered ship becomes a total loss or is accepted by her hull or war risks underwriters as a constructive total loss;

(iii) if the ship is reported missing, at noon UTC on the thirtieth day after the date of the last report of the ship;

(iv) if the managers have given notice of termination of cover, or notice of variation of rates or terms and there is no agreement as to the variation, at the end of the notice period given;

(v) if the managers have exercised their discretion to terminate the entry under rule 17(b), at the time and date specified by the managers, provided that the directors may at their absolute discretion and upon whatever terms they may think appropriate, determine otherwise.

(c) If a member's cover is terminated for any reason whatsoever in respect of any or all of his entered ships, then even after the termination the member, his successors in title, trustees in bankruptcy or liquidators remain liable to pay to the Association any amounts owed to the Association unless a release call has been paid in accordance with rule 21. These amounts and any subsequent amounts due in respect of future supplementary calls are payable within 30 days of issue of a debit note and interest is due on late payments in accordance with rule 20(c)(ii).

(d) If a member's cover is terminated in respect of any or all of his entered ships, liabilities occurring before date of termination will be covered notwithstanding the ending of cover; however if a member's cover is terminated because of non-payment of calls or any other debt to the Association, or because of any failure to comply with the rules, then the Association will not be liable to pay anything to the former member, his successors in title, trustees in bankruptcy or liquidators, even in respect of liabilities which arose before the date when the entry ended, save only that all liabilities of the Association under a Certificate of Financial Responsibility, provided in respect of the former member's entry, shall be met until the Certificate is cancelled by the United States Coast Guard following notice to them by the managers of the termination of cover.

(e) Notwithstanding the provisions of the above paragraph the directors have discretion to agree to make payments for former members who have been expelled from the Association, upon whatever terms they may think appropriate.

31 *Assignment*

A member cannot transfer any of his rights or duties in the Association to anyone else without the written consent of the managers, who may impose whatever terms or conditions they think appropriate in return for giving such consent. If no consent is given, rule 30(b)(i) will apply and the entry of the ship affected will terminate automatically.

32 Notices

Unless otherwise agreed with the managers any notice sent by a member to the Association or vice versa must be sent by telex or by fax. The notice will be deemed to be received in the case of transmission by fax, upon receipt of the fax message provided that the receiver's fax number is recorded on the sender's copy of the transmission.

Where a notice is sent by the Association or by the managers to a member recorded on a certificate of entry, notice sent to the first party named on the certificate of entry or to the broker (if the entry is made through a broker) will be treated as sufficient notice to the member concerned and to any other member concerned on the certificate of entry.

Notice to the Association must be given to Shoreline Mutual Management Ltd, fax no 071-606 1248, telex no 921567 PENSHP G.

33 Disputes

If any dispute arises between a member and the Association it must first be referred to the directors for a decision. Such a decision must be given within six months. If, after the directors have given their decision the member remains unsatisfied, then the dispute must be referred to arbitration in London by three arbitrators, one to be nominated by the member, one by the managers on behalf of the Association, and the third to be appointed by the arbitrators nominated by each party. The arbitrators are to be members of the London Maritime Arbitrators' Association, and the arbitration will be subject to the Arbitration Acts 1950-1979 and any statutory amendments, and the rules of the London Maritime Arbitrators' Association as published from time to time.

34 Law

These rules and any special terms of entry form a contract of insurance between the Association and a member, and are subject to English law and the Marine Insurance Act 1906.

Shoreline Correspondents

Penningtons

Royex House
Aldermanbury Square
London EC2V 7HD

Tel: 071-457 3000
Fax: 071-457 3240
Telex: 921567 PENSHP G
DX 33853 Finsbury Square
After hours: Hugh Bryant
0372 470284 tel. and fax
0374 275069 mobile

Le Gros Buchanan & Paul

2500 Columbia Center
701 Fifth Avenue
Seattle
Washington 98104-7051
USA

Tel: (206) 623-4990
Fax: (206) 467-4828
After hours: Craig Nodtvedt
(206) 882-0945

Wilmer, Cutler & Pickering

2445 M Street, NW
Washington, DC 20037-1420
USA

Tel: (202) 663-6909
Fax: (202) 663-6363

Hill, Betts & Nash

One World Trade Center
Suite 5215
New York, NY 10048
USA

Tel: (212) 839-7000
Fax: (212) 466-0514/
466-1896/466-1917
After hours: Michael J Ryan
(908) 276-9034

APPENDIX B

SHORELINE MUTUAL INSURANCE
TANKER AND NON-TANKER RATING SCHEDULES

:ND EDITION - JUNE 1994

SHORELINE

DRAFT

THIS DOES NOT CONSTITUTE AN OFFER OF INSURANCE.

TANKER RATING SCHEDULE

Based upon deadweight tonnage carrying capacity per voyage undertaken in US$ per deadweight ton. Age will be deemed to that applicable at the commencement of the Shoreline policy year in question.

Age of Ship:	<5	6-10	11-15	16-20	21-25	>25
Dirty Oil (conventional construction)	0.61	0.64	0.67	0.70	0.73	0.76
Clean Oil (conventional construction)	0.25	0.26	0.27	0.28	0.29	0.30
Dirty Oil (mid-deck construction or double-bottom)	0.54	0.57	0.60	0.63	0.66	0.69
Clean Oil (mid-deck construction or double-bottom)	0.22	0.23	0.24	0.25	0.26	0.27
Dirty Oil (double skin)	0.50	0.52	0.54	0.56	0.58	0.60
Clean Oil (double skin)	0.19	0.20	0.21	0.22	0.23	0.24

Surcharges to be applied to the above:-

1 Inland tank barges carrying no more than 30,000 barrels of oil in no more than 12 tanks to be charged at 65% of the above rates;

2 Any fleet with a ship which has spilled up to 100 barrels in a single incident within the EEZ of the USA, or has on average spilled up to 50 barrels per ship, within the last 5 years preceding the start of the Shoreline policy year in question, plus 5%;

3 As (2) above, but 100-250 barrels in a single incident or 50-125 barrels average per ship, plus 10%;

4 As (3) above, but 250-500 barrels in a single incident or 125-250 barrels average per ship, plus 15%;

5 As (4) above, but 500-750 barrels in a single incident or 250-375 barrels average per ship, plus 20%;

6 As (5) above, but over 1,000 barrels in a single incident or over 375 barrels avorage per ship, rating to be specially referred to the Shoreline directors for individual assessment.

sue/shorel2(4)

SHORELINE MUTUAL (BERMUDA) LTD

DRAFT

THIS DOES NOT CONSTITUTE AN OFFER OF INSURANCE

NON-TANKER RATING SCHEDULE 15th JULY 1994

Based upon gross tonnage. Rates are annual advance calls in US$.

Size of ship:

<1,500	3,000
1,500-10,000	3,500
10,001-30,000	4,000
30,001-50,000	4,500
>50,000	5,000

Surcharges to be applied to the above:

1 Any fleet with a ship which has spilled up to 100 barrels in a single incident within the EEZ of the USA, or has on average spilled up to 50 barrels per ship, within the last 5 years preceding the start of the Shoreline policy year in question, plus 5%;

2 As (2) above, but 100-250 barrels in a single incident or 50-125 barrels average per ship, plus 10%;

3 As (3) above, but 250-500 barrels in a single incident or 125-250 barrels average per ship, plus 15%;

4 As (4) above, but 500-750 barrels in a single incident or 250-375 barrels average per ship, plus 20%;

5 As (5) above, but over 1,000 barrels in a single incident or over 375 barrels average per ship, rating to be specially referred to the Shoreline directors for individual assessment.

sue/shorel2(4)
July 1994 Edition

APPENDIX B-2

APPENDIX C

LETTER DATED DECEMBER 1, 1993 FROM MR. DAN SHEEHAN, DIRECTOR OF THE NATIONAL FUNDS POLLUTION CENTER

U.S. Department of Transportation
United States Coast Guard

Director
United States Coast Guard
National Pollution Funds Center

4200 Wilson Blvd., Suite 1000
Arlington, VA 22203
Staff Symbol: (c)
Phone: (703) 235-4700

91-025

16450

DEC 1 1993

Mr. Hugh Bryant
Penningtons
Royex House
Aldermanbury Square
London EC2V 7HD
England

Dear Mr. Bryant:

Your letter of November 22, 1993 requests the National Pollution Funds Center's approval, in principle, of the "Shoreline" scheme as outlined in your letter. Please consider this letter as such conceptual approval.

One purpose of "Shoreline" would be to serve as a financial responsibility guarantor under the Coast Guard's Notice of Proposed Rulemaking (NPRM) published September 26, 1991. As you know, there has been no decision taken on whether to adopt the NPRM as a final rule.

Accordingly, this letter does not constitute approval of "Shoreline" as an insurance guarantor for purposes of Coast Guard regulations. Within this constraint, however, we see no reason why "Shoreline" could not become an acceptable insurance guarantor. Fundamental to a final determination would be an analysis of the company's financial documents, its organization, reinsurance program, and management. The enclosed list of questions will assist you in developing the information we ultimately would ask of "Shoreline" with respect to actual approval. This list reflects the information required of any entity seeking to become an acceptable insurance guarantor.

Sincerely,

D. F. Sheehan

D. F. SHEEHAN
Director, National Pollution Funds Center

Encl: (1) List of Questions

LIST OF QUESTIONS

1. Insurer's most recent, independently audited, financial statements (e.g., balance sheet and income and expense statement).

2. Description of method to be used to reinsure U.S. water pollution risks, including the names of the reinsurers and the amount of retention.

3. Date of incorporation, history as an insurer, and experience of the officers and managers.

4. Whether the insurer has ever refused to satisfy any judgements awarded in the U.S. or elsewhere. If so, please cite the cases.

5. If a P&I Club, is the Club's administrative and operating procedure similar to that of P&I Clubs in the International Group? Please explain.

6. What type and size (gross tons) vessels would be insured for U.S. water pollution risks.

7. Is insurer prepared to act as a guarantor and comply with the U.S. Coast Guard regulations implementing OPA 90?

8. Does the insurer write insurance in any other countries? If so, please explain.

9. Who will be authorized to execute insurance guaranties on behalf of the insurer?

10. Who will be the insurer's U.S. agent for service of process?

11. What form of Government oversight will apply to the insurer at its place of incoporation and elsewhere?

After examination of the above requested information, further details might be required.

Appendix C-2

APPENDIX D

LETTER DATED JULY 19, 1994 FROM THE REGISTRAR OF COMPANIES

Registrar of Companies
30 Parliament Street
Hamilton HM 12 - Bermuda

Telephone: (809) 295-5151
Telex: 3609 ACGEN BA
Facsimile: (809) 292-6640

In reply please quote the date of this letter and the following reference:

RC/INS/EC

19th July, 1994

The Honourable W. J. Tauzin, Chairman,
Sub-Committee on Coast Guard & Navigation
Committee on Merchant Marine & Fisheries
House of Representatives,
Washington D.C., 20515-1803,
U.S.A.

Dear Mr. Chairman:

Re: Shoreline Mutual (Bermuda) Limited ("Shoreline")

This will serve to confirm that the above captioned Bermuda mutual insurance company was incorporated pursuant to the terms of Part XII of the Bermuda Companies Act 1981 on 18th February, 1994.

Shoreline has been approved as an insurer for the purpose of the Bermuda Insurance Act 1978 subject to the completion of its reinsurance protections and a bond offering.

The management of Shoreline have kept us fully apprised of developments with respect to this project since its application was reviewed by the Bermuda Insurers' Admissions Committee in February of this year.

We fully anticipate that Shoreline will meet the conditions referred to above and that it will be fully operational and licenced as a matter of Bermuda law so as to be in a position to guarantee Certificates of Financial Responsibility for tankers by 28th December, 1994 as required by your recently promulgated interim final rule.

Please do not hesitate to contact me if I can be of any further assistance to you in respect of Shoreline.

Yours faithfully,

Malcolm Butterfield
REGISTRAR OF COMPANIES

MB/pvd

WILLIS FABER NORTH AMERICA, INC.
REINSURANCE INTERMEDIARIES

Wall Street Plaza
New York, NY 10005-1843
Telephone 212-344-7600
212-820-7600
Facsimile 212-344-4646

July 20, 1994

Mr. Hugh Bryant
Penningtons
Royex House
Aldermanbury Square
London EC2V 7HD

RE: Shoreline Mutual (Bermuda) Ltd

Dear Hugh:

We would like to take this opportunity to bring you up-to-date on our activities as Shoreline's appointed Reinsurance Intermediary and also share with you some of our observations which we have formulated over the past thirty days.

As you are aware, we have developed an information report to reinsurers which outlines the history of OPA and focuses on the development of Shoreline. This report provided our readers with what we feel to be an accurate depiction of key issues surrounding the challenges which are in front of us with respect to certificates of financial responsibility and vessel owner's pollution liability insurance requirements. At this stage we have restricted our approach to a limited number of potential reinsurers in diversified geographical locations. This exercise has allowed us to develop input from some key reinsurance markets, with different backgrounds, who have provided us with insight and in most cases support for the continued development of a reinsurance program for Shoreline. The major geographical reinsurance areas which we have targeted include the U.S.A., London (including Lloyd's), Bermuda, Continental Europe and Australia. While this preliminary marketing exercise was clearly to develop support we also wanted to establish if there existed any inherent reasons why the reinsurance community would not be in a position to support and provide the full capacity for Shoreline's proposed reinsurance program. We are pleased to report that while there are some markets that will not be in a position to support this reinsurance program. the vast majority do not see any limitations with the nature of our proposed program. In fact, although this marketing exercise was very limited, we have already received both written and verbal indications of potential conventional and finite capacity in excess of $150,000,000. We feel that this amount of capacity from a limited number of markets supports our confidence in supplying Shoreline with a viable reinsurance program.

It was just as important for us to establish any reasons why certain reinsurance companies would not support Shoreline. We would like to outline the main reasons which can be discussed in more detail at a later date:

a) Accumulation of exposures - some reinsurers already participate on the International Group of P & I Clubs reinsurance protections. Not knowing how the P & I Clubs are ultimately going to deal with these exposures they did not want to commit to a possible doubling up of aggregate exposure.

b) Fear of reprisal - some reinsurers were concerned that if they supported Shoreline they would not be allowed to continue to support the excess pollution covers (considered to be very profitable business) currently controlled by the P & I Clubs.

c) Direct action - one reinsurer did not want to lend credence to legislation calling for direct action and absolute liability.

d) Pollution Liability - due to the nature of pollution liability, several reinsurers have excluded coverage for this class of business entirely (of course the reason for this is "onshore" pollution losses in the past).

e) Increased Loss Costs - one reinsurer was concerned that the implementation of N.O.A.A. Regulations on National Resources Damage suggests that virtually every spill will result in *substantial* payments without actual damage.

As mentioned previously, even without the reinsurers who expressed above concerns there is ample capacity in today's market to meet Shoreline's requirements, however, if some of these issues clear themselves up, i.e. how are the P & I Clubs going to use their existing reinsurance program, then even more capacity would be available to us.

We would like to express that both Willis Faber North America, Inc. and Willis Faber and Dumas, Ltd., the reinsurance arms of Willis Corroon Group, are prepared to devote substantial resources to provide Shoreline with the most effective reinsurance program. As you are aware, the Willis Corroon Group is one of the world's top five insurance brokerage firms and second largest reinsurance firm with 310 offices and over 11,000 employees worldwide.

WILLIS FABER NORTH AMERICA, INC.
REINSURANCE INTERMEDIARIES

We will continue our efforts and keep you advised.

Sincerely yours,

George P. Reeth, Jr.
Executive Vice President & Chief Executive Officer
Marine, Aviation and International Department

GPR/mk

cc:	Chris Clark	011-44-71-488-8642
	Neil Lowney	(212) 504-9769
	Julian Wade	011-44-71-481-4361

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Testimony of
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on behalf of

Greek Shipping Co-operation Committee, London, United Kingdom
Union of Greek Shipowners, Piraeus, Greece
Norwegian Shipowners' Association, Oslo, Norway
Swedish Shipowners' Association, Gothenburg, Sweden

before

Subcommittee on Coast Guard and Navigation,
Committee on Merchant Marine and Fisheries,
House of Representatives,
Congress of the United States of America.

Oversight Hearing,
Vessel Certificates of Financial Responsibility
Interim Final Rule

1334
Longworth House Office Building
Washington, D.C.
July 21, 1994

Mr. Chairman.

The Greek Shipping Co-operation Committee, Union of Greek Shipowners, Norwegian Shipowners' Association and Swedish Shipowners' Association are very grateful to you for your invitation to testify at this hearing today on the topic of the Interim Final Rule on Certificates of Financial Responsibility (COFRs) for vessels, issued on July 1, 1994, by the United States Coast Guard.

A. <u>Inadequate Insurance and Lack of COFRs</u>

The organizations which I represent here today have long been concerned about not only the lack of viable commercial products to meet the financial responsibility requirements of the Oil Pollution Act of 1990 (OPA) but also the inadequacy of pollution insurance currently available. With few exceptions, shipowners are unable to obtain pollution insurance at levels above $700 million and this limit is clearly inadequate in the face of virtual unlimited strict liability, arising under the Act, for the consequences of oil spills in the territorial waters of the United States.

In these circumstances, the shipowner who engages in the U.S. trades does so seriously underinsured and is, thus, unprotected

from overwhelming potential claims. This, in turn, leaves the Oil Spill Liability Trust Fund and the U.S. public at large seriously exposed for the potential uninsured and unrecoverable losses.

Accordingly, our organizations, have, for several years, been working together to propose a solution to both of the aforementioned problems, i.e., the problem of inadequate pollution liability insurance and the problem of finding a formula to secure financial responsibility certification meeting the requirements of OPA.

B. The Proposal

Our Associations have developed a solution that meets the needs of the international shipowning community as well as the needs of the U.S. Government and potential claimants under OPA. We propose that Congress enact legislation mandating that all tankers engaged in the U.S. international ocean going petroleum trades carry an aggregate of $2 billion in pollution liability insurance. We believe the mandatory nature of this insurance requirement to be an essential element of the formula, since owners taking out the high level insurance would be placed at a severe competitive disadvantage and, thus could not afford to do so, if other owners were permitted to go without it.

We, therefore, propose that Congress establish a non-profit, Government Sponsored Enterprise (GSE) to be known as the "Mandatory Excess Insurance Facility," (MEIF), to provide excess insurance, over and above amounts available in the market, whether from the Protection and Indemnity Associations (P & I Clubs) or from commercial sources, to an aggregate amount of $2 billion and also to issue guaranties for COFRs while meeting all of the requirements of OPA.

The MEIF would raise its initial capital of $2-3 billion by issuing bonds, as do other GSEs, through the Treasury auction system, and by initial deposit premia to be paid by the shipowners using the facility. The Bonds would be bought by private investors and paid off by way of revenue generated by premium income from shipowners trading their vessels to the United States. In the event of the

MEIF enjoying a favorable claims record, it is estimated that the initial debt would be retired within a period of ten years.

C. Practical Solution to Insurance and Certification Problems

Because we have been unable to find viable commercial solutions to these two problems and because the Coast Guard, as an agency of the Executive branch of the U.S. Government, lacks the authority to resolve them, we conclude that it is necessary to turn to the legislative branch for assistance. Recognizing the practical difficulties in enacting legislation to make such changes, we have embraced the following precepts in order to make the proposal workable:

* The MEIF proposal would not amend OPA or diminish its protection in any way.
* It would not involve any federal outlays or taxes.
* It could not be construed as a new federal program because it would be privately managed.
* It would be self supporting and not reliant on federal funding.
* Since the scheme would be independently capitalized, it would not conflict with or displace capacity for existing pollution coverage.
* The MEIF would be structured so that it could reinstate itself if it sustained a catastrophic loss.
* The MEIF would issue guaranties for COFRs meeting all requirements of OPA, including direct action.
* The MEIF would benefit claimants, would protect the Trust Fund against unrecoverable claims resulting from inadequately insured shipowners and would protect shipowners from ruinous liability not based on fault.

D. The MEIF and Coast Guard Rule

The Coast Guard issued the COFR Interim Final Rule on July 1, despite widespread industry concern that the required guaranties will not be available except on a very limited and selective basis. While we believe that the Coast Guard had very little flexibility in the issuance of these regulations, we have grave reservations

about whether the rule can be successfully implemented so as to avoid catastrophic disruptions to the maritime trade of the United States.

We are advised that the Coast Guard's assurances to the effect that OPA protects guarantors from liability beyond their guaranty limits may be insufficient to allay the apprehensions of potential guarantors. While the Coast Guard may issue an interpretation of the effect of OPA section 1016(g), (limitation on a guarantor's liability), we are advised that there is no basis for insulating guarantors from liabilities arising under other laws as a consequence of being a direct action guarantor. Our advice is that such exposures may exist not only for pollution claims, but also for collateral claims and punitive damage awards, such as bad faith refusal to settle. The fact is that the exposure remains and shipowners (and their P & I Clubs) are not prepared to risk their capital for such a large and unpredictable exposure. We are less confident than the Coast Guard that the proposed commercial alternatives cited in the preamble to the Interim Final Rule and in the Regulatory Impact Analysis will work. Our organizations have worked for several years to develop a fiscally sound proposal for COFRs and excess insurance for tankers trading to the United States. We attest to the great difficulty in finding capital for such a facility, in finding reinsurance capacity without displacing capacity relied upon by existing pollution insurers, and in arranging for reinstatement of the facility in the event of a full limit loss. These were all questions which were faced and resolved in the developments of the MEIF proposal.

We urge this subcommittee to insist that the financial integrity of any insurance product (including the MEIF), which shipowners may be forced to purchase in order to comply with the financial responsibility requirements under OPA, be scrutinised rigorously. This would include examination of capital structure and loss reserves, the ability to meet and service claims, and the capacity to reinstate the cover in the event of the occurrence of a full limit loss.

E. Conclusion

As previously stated, our primary interest in developing the MEIF proposal was and is to address the issue of uninsured liability exposure, and we note that the Coast Guard's Regulatory Impact Analysis[1] views the MEIF as meriting further study for dealing with this issue.

We offer the MEIF, however, to the U.S. Government and public as an *immediate solution* to the two related problems - lack of adequate, affordable excess insurance and lack of a proven means of meeting COFR requirements. Although the Coast Guard discarded the MEIF as a solution to the latter problem because it was considered to be principally focused on the former and also because of the need to enact legislation, we strongly believe that any solution to the COFR issue which does not also address the excess liability issue will only survive until the next serious pollution incident. Moreover, we believe that, if Congress does not act now to address both issues, it may well be called upon to revisit the situation later when the proposed alternative solutions to the COFR problem do not succeed.

The complete MEIF proposal, together with proforma financial statements and a draft legislative proposal, is attached hereto to be made part of the record.

The MEIF is a proposal which meets the demanding requirements of fiscal soundness, commercial feasibility and consistency with the objectives of OPA. It is a fair, effective and durable solution to the twin problems of COFRs and underinsured shipowners. The proponents of the MEIF, the Greek Shipping Co-operation Committee, Union of Greek Shipowners, Norwegian Shipowners' Association and Swedish Shipowners' Association urge the United States Congress to consider this proposal on an accelerated basis and to enact legislation providing for a mandatory excess insurance facility.

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[1] The RIA at page 107 refers to an earlier version of the MEIF which proposed that the Oil Spill Liability Trust Fund and importers of petroleum participate in the capitalization of the facility. Those provisions have been deleted and it is currently proposed that capitalization of the facility come entirely from a public debt offering and initial deposit premia paid by the shipowner users of the MEIF.

Our proposal also has the support of INTERTANKO and the Baltic and International Maritime Council (BIMCO). We would be pleased to work with any committee or agency of any branch of the United States Government, in any appropriate fashion, aimed at bringing this about.

PROPOSAL FOR A MANDATORY EXCESS INSURANCE FACILITY

JUNE 17, 1994

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The members of the associations behind this joint proposal, namely

Greek Shipping Co-Operation Committee
Union of Greek Shipowners
Norwegian Shipowners' Association
Swedish Shipowners' Association

control 64 mill. dwt. oil tanker tonnage. This constitutes 31% of the world's oil tanker tonnage, and 48% of the independent (non-oil company) oil tanker tonnage in the world.

It is estimated that approximately 30% of US oil import is carried on tanker tonnage controlled by the members of the above-mentioned associations.

This material is prepared by LeBoeuf, Lamb, Greene & MacRae, 1875 Connecticut Avenue, N.W., Washington, D.C. 20009, on behalf of Norges Rederiforbund (Norwegian Shipowners' Association), Radhusgaten 25, N-0116 Oslo, Norway, and Dyer, Ellis, Joseph & Mills, 600 New Hampshire Avenue, N.W., Washington, D.C. 20037, on behalf of the Greek Shipping Cooperation Committee, #6 Middlesex Street, London E1, U.K. Both LeBoeuf, Lamb, Greene & MacRae, as an agent for the Norwegian Shipowners' Association, and Dyer, Ellis, Joseph & Mills, as an agent for the Greek Shipping Cooperation Committee, are registered with the Department of Justice, Washington, D.C. under the Foreign Agents Registration Act. This material is filed with the Department of Justice where the required registration statements are available for public inspection. Registration does not indicate approval of the United States Government.

JOINT PROPOSAL FROM
GREEK SHIPPING CO-OPERATION COMMITTEE,
UNION OF GREEK SHIPOWNERS',
NORWEGIAN SHIPOWNERS' ASSOCIATION
AND SWEDISH SHIPOWNERS' ASSOCIATION

I. SUMMARY OF THE MANDATORY EXCESS INSURANCE FACILITY (MEIF)

A. THE BASIC CONCEPT

Mandatory oil pollution insurance of $2 billion aggregate would be required for all tankers importing oil to the United States. (A domestic regime should be developed with the assistance and cooperation of US owners.)

In the absence of commercial insurance to meet this requirement, the Secretary of Transportation would establish a government-sponsored, federally-chartered, private oil pollution insurance facility that would be capitalized with the assistance of public borrowing authorities. The facility would be self-sustaining, deriving its on-going financial support from mandatory premiums paid on ships transporting oil to the United States.

The facility would have two distinct functions: first, it would provide excess insurance above what is available in the marketplace. If $500 million is available through the P&I Clubs, the facility would provide pollution coverage in excess of $500 million up to $2 billion per accident. Second, it would act as a guarantor under section 1016 of the Oil Pollution Act of 1990

("OPA 90") with certain recourse rights against the shipowners who would seek recovery from their Protection and Indemnity ("P&I") club under the standard P&I terms. These guarantees would support Certificates of Financial Responsibility (COFRs) required by OPA 90.

The facility would be available on a voluntary basis to non-tank vessels for the purpose of obtaining COFRs. However these comments focus on tank vessels.

B. THE MANDATORY EXCESS INSURANCE FACILITY (MEIF)

To create the additional capacity needed to meet the mandatory insurance requirement, Congress would authorize the Secretary of Transportation to charter a "government sponsored enterprise" ("GSE") that would be in the form of a non-profit, tax-exempt, mutual insurance company with no effect on the Federal Budget (hereinafter referred to as "MEIF").

MEIF would secure the capital required to cover full limit losses through the collection of premiums and offerings of debt securities to be issued through the Treasury marketing system established for GSEs.

MEIF would be managed by a board of directors, a majority of whom would be elected by the policyholders. The directors would include representatives of the marine insurance industry, federal agencies and other parties as appropriate.

C. THE FINANCING OF THE FACILITY

MEIF could be initially financed by deposit voyage premiums from policyholders (the shipowners) and a $2 billion offering of debt securities to be issued through the Treasury marketing system established for GSEs. The debt is projected to be repaid within ten years, provided no loss occurs, rendering the MEIF

independent of the implicit Federal guarantee associated with GSE obligations when that debt is retired.

MEIF would mainly derive income and accumulate reserves from the mandatory premiums paid by the shipowners and assessed on a per-ton, per-voyage basis on imported oil into the United States. The premiums from the shipowners (estimated to amount to an annual total of up to $350 million (see page 11)), would be designed to be included in Worldscale[1] or otherwise reimbursed by the charterers and ultimately passed on to the consumer. The company is also likely to generate substantial investment income which over time should facilitate the retirement of MEIF debt within ten years provided no loss occurs and, ultimately, the reduction of the mandatory insurance premiums.

D. THE OPERATION OF MEIF

MEIF would set premiums through an underwriting committee made up of individuals with expertise in underwriting and evaluation of pollution risk.

MEIF will begin operations with financial resources sufficient to pay at least one full-limit claim and to sustain the operations of the facility. Timely availability of such financial resources will be secured by the initial issuance of debt securities. Should multiple claims occur, government authorization would allow MEIF to retain the ability to issue additional debt to meet the claims obligations.

MEIF as a provider of insurance would follow the form of coverage of the P&I clubs. However, as a COFR guarantor, MEIF would have

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[1] Worldscale is an internationally agreed formula for determining voyage rates.

to pay claims, subject to OPA 90 limits, that might not be compensable under the clubs' rules and conditions.

In order to minimize the administrative overhead of MEIF, premium collection and claims handling could be performed by the P&I clubs or other appropriate existing organizations acting as agents for MEIF which would thus benefit from professional marine insurance expertise.

The benefits of a positive claims experience would be passed on to the US consumers in the form of lowered insurance premiums rather than dividends to the shipowners.

E. THE PUBLIC POLICY BENEFITS

The government solves the COFR problem without compromising the direct access features of OPA 90.

Providing insurance in the aggregate of at least $2 billion offers incentives for responsible shipowners to return to or remain in the US trades, including owners with a large capital base and quality presence in this market.

The availability of excess insurance will facilitate the financing of new double hull tankers to replace the aging fleet.

The U.S. government, taxpayers, and cargo interests would have an additional $1.5 billion buffer between claims and the Trust Fund.

The facility would internalize the MEIF costs in the United States rather than "stealing" capacity from international markets.

II. MEIF DETAILS

The following discussion sets forth a proposal to establish a marine oil pollution insurance company (the "Company") that would enable shipowners to meet the financial responsibility requirements of OPA 90, as well as other federal and state environmental laws and to provide excess insurance well above the capacity of the commercial market. This proposal reflects the consensus of the independent shipowners represented by the Greek Shipping Cooperation Committee ("GSCC"), the Union of Greek Shipowners ("UGS"), the Norwegian Shipowners' Association ("NSA") and the Swedish Shipowners' Association ("SSA"). It is presented in question and answer format to reflect the issues considered by the participants in this effort.

A. CORPORATE ORGANIZATION, CAPITALIZATION AND FUNDING

1. Basic Structure

The company would be organized pursuant to an Act of Congress as a not-for-profit, tax-exempt, federally-chartered, government sponsored enterprise. Otherwise, the facility would take the form of a privately-owned mutual insurance company. Initial capital would be raised through collection of premiums payable in advance and a $2 billion debt offering. We believe that this combination of financing will provide the best chance of success.

Questions:

Why is legislation by Congress required?

First, it appears that the commercial market place is presently unable to provide generally either the additional insurance capacity to provide sustained pollution coverage in excess of the present basic P&I policy of $500 million or the guarantees required by section 1016(b) of OPA 90. Consequently, federal

government assistance is required to aid in the massing of the necessary capitalization for additional capacity and to secure the necessary premium flow on a universal base. Second, OPA 90 and other related laws do not authorize the Executive Branch to establish such an entity.

Would this legislation amend OPA 90 or in any way diminish its protections?

No, the legislation would amend the Ports and Waterways Safety Act, not OPA 90. The legislation would provide better protection for the environment by offering additional insurance coverage for claimants from owners whose loss of limits and exhaustion of P&I cover might otherwise result in claims against the Oil Pollution Liability Trust Fund. It would enable the Coast Guard to implement COFR requirements without compromising the direct action features of section 1016 of OPA 90. It would also provide the necessary assurance of financial security that would prompt investment in the new generation of double hull tankers.

What is a mutual insurance company?

A mutual company issues no stock but rather is owned by its policyholders. This ownership interest is actually quite limited since it cannot be sold or transferred and terminates when the insurance policy is cancelled. The main attributes of ownership are the right to vote for election of directors. In this case, policyholders would not receive dividends, nor have any liability for supplementary calls in contrast to their position as P&I club members. Even if the company were to become insolvent, policyholders would risk losing nothing more than their premiums paid for current coverage.

Premiums would be set at the beginning of each policy period (normally 12 months) and prepaid prior to each voyage. Policyholders would not be assessable for additional premium

calls. However, losses could influence the MEIF-financing costs and cause an increase in future voyage premiums.

Are there precedents for this type of government-chartered insurance program?

Yes, there are several federal precedents where the commercial insurance markets were unable to provide sufficient insurance that was deemed necessary to protect important public interests. These precedents include the Overseas Private Investment Corporation, the Federal Crop Insurance Program, the Vessel and Aviation War Risk Insurance Program, the Federal Deposit Insurance Corporation, and the College Construction Loan Insurance Association (also a GSE).

Who would actually run this insurance company?

The Secretary of Transportation would "launch" the insurance facility because the insurance market could not generally provide the mandatory levels of insurance. The governing board would be appointed from the private sector according to the terms of the statute. It is contemplated that the initial board of directors would be drawn from the marine, energy, and insurance industries. Government representatives would also be appointed to the board. When the board is constituted the company would begin business as a private corporation with private sector employees, in the same manner that similar government-sponsored enterprises work, such as the College Construction Loan Insurance Corporation and the Federal Home Loan Mortgage Corporation.

2. Capitalization

It is estimated that MEIF will require at least $2 billion in initial secured capitalization. Thereafter, the MEIF would make such bond issues only if a succession of major spills were to deplete its resources. The capital would be provided by debt

financing in the form of bonds issued by the new corporation through the government agency securities market. Like obligations of other "government sponsored enterprises", these would probably receive favorable market ratings and trade at a slight premium over Treasury issues. Although not backed by the full faith and credit of the government, these issues are perceived by the financial markets as having an effective government guarantee. Consequently, these securities typically enjoy favorable bond ratings. Funds for repayment of the debt would be provided by mandatory premium revenues.

Questions:

Do other government-sponsored insurance facilities have the authority to issue securities

Yes, for example the Federal Crop Insurance Program contains authority for the President to issue up to $1 billion in debt and $500 million in stock.

Would this debt count toward increasing the federal deficit?

No, the legislation would establish the facility as an off-budget entity, such as the Construction Loan Insurance Association, the Federal Home Loan Mortgage Corporation, or the Farm Credit Banks. Each of these is a "government sponsored enterprise", i.e., a privately-owned but government-sponsored corporation that issues its own bonds in the government agency market. These borrowings are excluded by law from computation of the national debt.

When would these public offerings be made?

Once the company is chartered by the government, it would raise all of the required capital (a minimum of $2 billion, preferably $3 billion) immediately so that when the facility first issued policies it would have its funding in place. The timing and

terms of the offering would have to be coordinated through the Treasury Department, as are other offerings by GSEs. The Company would have the authority to engage in further financing; however, unless additional funds were required to meet catastrophic losses, MEIF would not issue further debt.

Is there likely to be a market for these bonds?

The securities of the GSEs have been successfully issued for many years. Although not backed by the full faith and credit of the federal government, they are generally regarded as investment grade instruments. The premiums provide a reliable income stream to meet these obligations.

In general, GSEs operate through a fiscal agent that serves the function of a lead underwriter in coordinating securities offerings. Debt securities are marketed through a selling group composed of government securities dealers and banks and having from five to 100 members. Selling group members receive a concession, a percentage of the face amount of securities placed, as compensation for their effort. The selling group members are also expected to support secondary trading in the GSE's securities. Generally the selling group members do not purchase bonds for their proprietary trading accounts but rather seek to achieve a broad-based distribution of the securities.

3. Shipowner Participation through Premiums

Funds would also be provided by insured shipowners by payment of initial deposit premiums, but mainly by future voyage premiums.

How would future voyage premiums be collected?

Prior to purchasing insurance from MEIF, the shipowner would be required to pay a deposit premium in an amount equal to the

highest voyage premium likely to be paid by the owner in a given policy year. This deposit would be held by MEIF as security for payment of future voyage premiums until the coverage is no longer required by the owner and is terminated.

There is an existing system among the P&I clubs for the collection of voyage premiums for trading to the United States. As the Regulatory Impact Analysis confirms, the club system covers over 95 per cent of the world sea-going tonnage. The P&I clubs therefore could serve as agents of MEIF for the collection of the voyage premiums from the shipowners.

This amount would in turn be collected by the shipowners from the charterers as part of the ordinary freight and be billed through the normal channels. It is expected that the excess pollution premium would be built into the Worldscale, as is the P&I club surcharge, and collected through these commercial channels.

A strict policing of the system is required in order to assure that no shipment of oil enters the United States without being charged with the voyage premium. Voyage premiums preferably should be paid in advance by the shipowners prior to the vessels entering the EEZ of the United States; however, if valid operational reasons prevent this, the shipowner would have to notify MEIF (via the agent) prior to the vessel's entry into the EEZ, permitting MEIF to invoice the shipowner and it, in turn, the charterers for the voyage premium. Any shipowner failing to notify MEIF of the ship's entry would have forfeited its MEIF insurance protection and would be exposed to full reimbursement to MEIF of any COFR guaranty claims payment. In the event of a failure to pay the voyage premium on time, MEIF would draw on the deposit premium accordingly and notify the shipowner to replenish the deposit premium until it reaches its full amount. Any shipowner failing to notify MEIF of the ship's entry or to replenish the deposit premium on time would have forfeited MEIF insurance protection and would be exposed to full reimbursement

to MEIF of any COFR guaranty claims payment. In the event of a failure to replenish the deposit premium, MEIF would notify the U.S. Coast Guard for the purpose of triggering withdrawal of the COFR.

Who would pay for the additional insurance?

The premium would be similar in nature to the voyage premium currently being charged for trading to the United States. This surcharge is currently included in the Worldscale system, and is therefore included in the cost of the cargo which ultimately is passed on to the consumer.

How much would this cost the consumer?

At this stage the determination of the premiums to MEIF is uncertain. It is proposed, however, that the computation of the voyage premium is based upon $1 per ton of cargo on board which (for illustration purposes) equals $0.14 per barrel and about $0.004 per gallon of gasoline paid by the consumer.

For the shipowner this amounts to a voyage premium of about $300,000 (for a VLCC of 300,000 dwt) or a total of annual premium payments from the ship owners of about $350 million per year.

4. Private Ownership of the MEIF

In this proposal, we do not anticipate issuing stock to the shipowners who are insured by the facility. Instead, the company would be what is called a mutual insurance company, which means that the ownership of the company is in the hands of the policyholders. The policyholders would have all voting rights and elect the non-government members of the board. Presumably proxy voting would allow an effective exercise of voting rights on behalf of the owners.

B. INSURANCE PROGRAM

1. Basic Terms of Coverage

MEIF would insure shipowners against liability under OPA 90, other federal and state environmental laws, and common law with respect to an accidental discharge of oil into the marine environment in excess of P&I club limits. The scope of coverage would be, except for financial responsibility guarantees under OPA 90, co-extensive with P&I coverage, i.e., terms of excess insurance coverage, with some adjustment, potentially would be identical to those offered by the underlying P&I club policy.

The P&I clubs would continue to provide indemnity insurance as they do today and would continue to be entitled to apply the "pay to be paid" principle, i.e., to require that the shipowner must pay the claimant from its own funds and thereafter seek reimbursement. Each club management would still determine what is compensable under its rules. Generally, the MEIF would follow club policy on coverage matters.

In no event would the MEIF insurance substitute for the P&I cover; it is excess insurance available to supplement the P&I Club cover only after full exhaustion of the club coverage. Therefore, in the event that P&I policy defenses are successfully applied by the P&I club due to the shipowner's breach of the P&I policy, the MEIF would not provide insurance denied by the P&I clubs on a primary basis. Additionally, a shipowner in breach of his P&I policy, would not be eligible to claim his MEIF coverage, even if all other MEIF policy conditions have been met.

COFR guarantees provided by MEIF under OPA 90 cause the guaranty liabilities to be determined by OPA 90 without regard to the MEIF insurance terms and would apply from the first relevant dollar up to the limit provided in OPA 90. The shipowner would be contractually obligated to reimburse the MEIF for any payment

made by the MEIF as COFR guarantor. In cases where the shipowner is fully covered by his P&I insurance policy, the MEIF would be reimbursed by the shipowner, who would seek recovery from his P&I club. Because the MEIF is acting as a guarantor, not an insurer, it is believed that this arrangement would not violate P&I Club provisions against double insurance. However, in cases where the MEIF pays guaranty claims falling outside the normal P&I insurance cover, the MEIF bears the risk of loss up to the insured's OPA 90 limits.

Responsibility for the layers of coverage up to the $ 2 billion limit can be illustrated graphically by the chart on the following page.

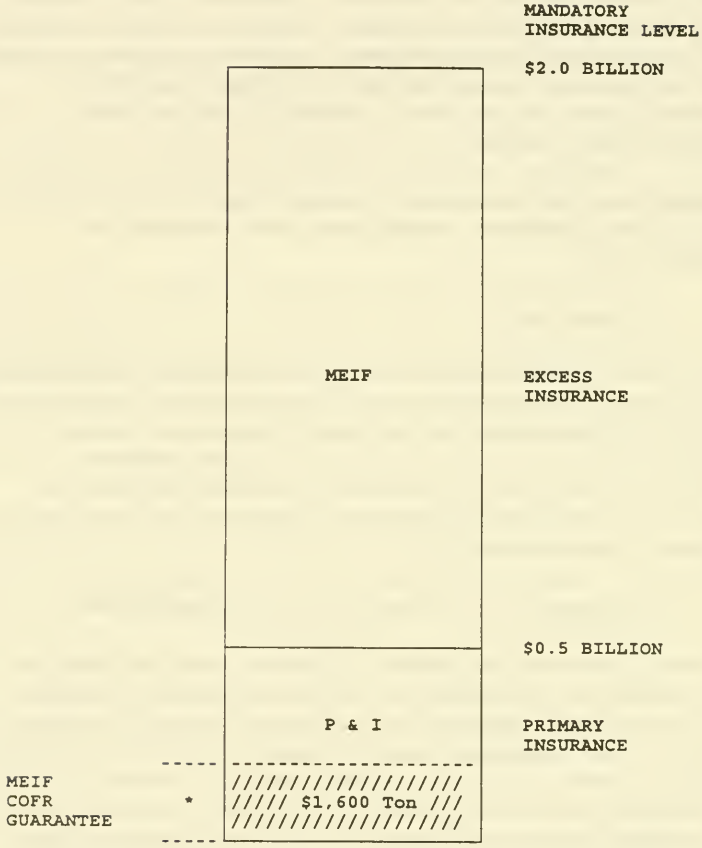
2. Policy Limits

Losses would be insured up to a mandatory assessable amount of $2 billion with a retention that would be equal to the underlying standard P&I coverage during any given policy period (e.g., insurance coverage by MEIF would be $1.5 billion where the insured has $500 million of underlying coverage through a P&I club). The voyage premium would be commensurate with the amount of coverage provided by MEIF.

3. Coverage of U.S. domestic Fleet and non-Tankers

In order to address the question of US-flag Jones Act carriers, all Jones Act tank vessels, over a certain tonnage and carrying oil and petroleum, might be included in the mandatory insurance program. This would permit equal treatment of the larger vessels in the US trades (such as the Alaskan trades). However, it would be necessary to exclude the smaller inland and coastal Jones Act tank vessels which do not require $2 billion in coverage. The details of this element are best left to be proposed by the affected US interests. In addition, MEIF could issue OPA 90 guarantees to non-tank vessels required to meet OPA 90's

LAYERS OF INSURANCE COVERAGE
FOR OIL POLLUTION LIABILITY



* COFR issued by MEIF may be required under OPA to cover damages outside P & I Club coverage.

financial responsibility requirements. However, excess insurance coverage is not envisaged for non-tank vessels at the present time due to the differences in the underlying potential for catastrophic oil spill risk.

4. Premium Structure

Premiums would be assessed by an underwriting committee of MEIF on the basis of a fixed rate per ton of oil for each voyage performed under OPA 90 jurisdiction. It is intended that this standard rate per ton would be incorporated into Worldscale as has the P&I club surcharge for US voyages. Any insured incurring a loss would be subject to higher premiums in the subsequent two years, as an additional incentive to avoid losses.

Dividends would not be paid on the insurance policies. Rather, favorable experience would be reflected in lower premium rates once MEIF has sufficient surplus assets.

5. Full Limit Losses and Reinstitution of Cover

MEIF would have as a goal holding sufficient surplus assets (partly in liquid investments and partly in prepared and committed credit lines) to cover two full limit losses (i.e., $3 billion). Assets would be derived from voyage premiums (which would accumulate in years in which no loss penetrates MEIF's layer of coverage), and authorized borrowing. It is also possible that MEIF may not have sufficient assets to cover claims in the unlikely event of multiple catastrophic losses in the same year. In any year in which the aggregate losses from all reported occurrences exceed or materially deplete MEIF's surplus assets, MEIF must be authorized to resort to borrowing through the issuance of additional bonds. In order to assure shipowners that MEIF's assets will not be depleted while their policies are in force, the government must commit to support MEIF through additional borrowings.

C. MANAGEMENT AND OPERATIONS

1. Role of Government

MEIF's initial directors would be appointed by the Secretary of Transportation in accordance with qualifications established by the enabling legislation. The directors appointed by the Secretary of Transportation would include individuals from interested governmental departments and individuals experienced in the maritime insurance industry. Within one year after insurance policies are issued by the MEIF, the policyholders would be entitled to elect additional directors comprising a majority of the board. It is likely that the private sector board members, who would be elected by the insureds, would be drawn from different parts of the marine industry. The criteria for representation on the Board should be set forth in bylaws when MEIF is organized. An underwriting committee appointed by the insureds would make proposals regarding coverage, insurability, premiums and claims. The government would retain an oversight role in the operation of MEIF as it does in other government-sponsored insurance enterprises, among other things, to ensure MEIF is not controlled by the Board in an anti-competitive manner.

2. Operations

To the extent that MEIF's operations do not justify a full-time staff, it may rely on independent expertise for both insurance and investment advice. MEIF would have substantial assets for investment, and investment income could eventually become a substantial source of income. Initially, it is expected that at least part of MEIF's assets would be invested in US government obligations. In the future, MEIF may wish to diversify its portfolio provided a high degree of investment safety is observed. The tax status of MEIF and its participants would

impact this decision. The employees of MEIF, if any, would not be government scheduled (civil service) employees.

MEIF would also contract for claims handling services. There are several sources available, including the P&I clubs and/or the network of adjustors and attorneys assembled by the P&I clubs and the International Tanker Owners Pollution Federation Limited. The goal is to avoid duplication of services by the entities that share a common interest in responding to oil spills and to benefit from existing expertise.

D. CONCLUSION

The foregoing structure has been designed to make participation in MEIF attractive to the government, the claimants, the cargo owners, and the shipowners. The government should see this as a constructive step to ensure financial responsibility while giving it a measure of control over the terms of coverage. MEIF expenditures would not negatively impact the Federal Budget. The use of debt financing for initial capital is practical because insurance participation is mandatory and thus a future source of revenue to repay the borrowing is assured. Individual shipowners will have a reduced risk of potentially ruinous uninsured liability, which is necessary to attract investments for a renewal of the aging fleet and to secure the continuous presence in this market by the large and experienced owners. If there are no major spills in the near future, the financial burden of insurance will be diminished by reducing future premiums.

The proposal benefits cargo owners by increasing the amount of insurance coverage available to independent shipowners, thereby reducing the exposure to cargo interests in several coastal states. This further protects the Oil Spill Liability Trust Fund by providing additional compensation to the Trust Fund in the event the owner cannot pay liability incurred. Claimants would

stand better chances to recover claims due to increased level of cover and liquidity of capital.

The public, the Coast Guard, P&I Clubs, and the environmental community would benefit from solving the COFR problem without compromising any of the direct action features of section 1016 of OPA 90.

III. EXHIBITS

A. PRO FORMA FINANCIAL STATEMENTS

B. DRAFT LEGISLATIVE PROPOSAL

NOTES TO PRO FORMA FINANCIAL STATEMENTS

1. The accompanying statements have been prepared for illustrative purposes only. They do not represent a forecast or estimate of future results.

2. It has been assumed that premiums will be paid at a rate of $300 million per year by shipowners. No increase in premium rates has been provided for despite inflation in expenses, clean up costs or the incidence of losses. In the two years following a loss, the insured party incurring the loss will pay 150% of normal premium; it is assumed here that the additional premium will be between $1 million and $2 million per year. Although premiums will be paid on a per voyage basis, it is assumed for these purposes that all the premiums will be paid at the beginning of the year and that $225 million will be fully earned in the first year. This data does not reflect amounts expected to be paid as deposit premiums which would be in addition to regular premium amounts.

3. Administrative expenses have been shown at $5 million in the first two years, increasing to $13 million in the eighth due to expanded size, claims administration and inflation. Organizational expenses are not projected separately. If paid by the company they would be amortized as part of the administrative expenses. It is assumed that the company will not be subject to tax.

4. The company would issue bonds for $2.0 billion prior to the first year of operations. Interest on the bonds is assumed to be 7%.

5. The company is presumed to earn investment income of 7%, net of investment expenses, on its investment base (total assets at beginning of the year, plus premiums, less interest on the bonds, less administrative expenses).

6. In the no loss scenario, the company will be able to begin redeeming bonds at the end of the fifth year and to retire all bonds after the eighth year.

7. The loss scenario assumes losses of $1 billion in the first year and another loss of $1.5 billion in the third year. Losses could consist either of guarantee payments that are not recoverable or of insured losses in excess of the P&I Club coverage. These losses would be fully reserved in the year of occurrence and paid out partially at the end of the first full year following the loss and the rest at the end of the second year. In this case, the company would not be able to redeem bonds during the period illustrated.

Scenario I - No Losses

PRO FORMA STATEMENTS
(000,000's)

	End of Year							
	1	2	3	4	5	6	7	8
Income Statement								
Premiums Written	300	300	300	300	300	300	300	300
Less Unearned Premiums	75	0	0	0	0	0	0	0
Premiums Earned	225	300	300	300	300	300	300	300
Less: Losses	0	0	0	0	0	0	0	0
Interest Expense	140	140	140	140	140	105	70	35
Administration	5	5	7	8	10	10	12	13
Underwriting Income	80	155	153	152	150	185	218	262
Investment Income	151	172	195	219	245	239	237	236
Net Income	231	327	348	371	395	424	455	498
Balance Sheet								
Cash and Investments	2,306	2,633	2,981	3,352	3,247	3,171	3,126	3,124
Liabilities:								
Loss Reserves	0	0	0	0	0	0	0	0
Unearned Premium Reserve	75	75	75	75	75	75	75	75
Bonds	2,000	2,000	2,000	2,000	1,500	1,000	500	0
Total Liabilities	2,075	2,075	2,075	2,075	1,575	1,075	575	75
Surplus	231	558	906	1,277	1,672	2,096	2,551	3,049
Total Liabilities and Surplus	2,306	2,633	2,981	3,352	3,247	3,171	3,126	3,124

Scenario II - Losses in First and Third Years

PRO FORMA STATEMENTS
(000,000's)

	End of Year							
Income Statement	1	2	3	4	5	6	7	8
Premiums Written	300	301	301	302	302	300	300	300
Less Unearned Premiums	75	0	0	1	0	(1)	0	0
Premiums Earned	225	301	301	301	302	301	300	300
Less: Losses	1,000	0	1,500	0	0	0	0	0
Interest Expense	140	140	140	140	140	140	140	140
Administration	5	5	7	8	10	10	12	13
Underwriting Income	(920)	156	(1,346)	153	152	151	148	147
Investment Income	151	172	160	147	133	83	99	116
Net Income	(769)	328	(1,186)	300	285	234	247	263
Balance Sheet								
Cash and Investments	2,306	2,134	1,948	1,749	1,034	1,267	1,514	1,777
Liabilities:								
Loss Reserves	1,000	500	1,500	1,000	0	0	0	0
Unearned Premium Reserve	75	75	75	76	76	75	75	75
Bonds	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000
Total Liabilities	3,075	2,575	3,575	3,076	2,076	2,075	2,075	2,075
Surplus	(769)	(441)	(1,627)	(1,327)	(1,042)	(808)	(561)	(298)
Total Liabilities and Surplus	2,306	2,134	1,948	1,749	1,034	1,267	1,514	1,777

UNITED STATES MANDATORY EXCESS INSURANCE FACILITY ACT OF 1993

To require additional pollution insurance for tank vessels carrying oil as cargo engaged in the foreign trade of the United States and charter a nonprofit corporation to provide excess insurance not available in the private market to meet that requirement.

Sec. 1. **Short Title.** This Act may be cited as the "Mandatory Excess Insurance Facility Act of 1993."

Sec. 2. **TANK VESSEL POLLUTION INSURANCE REQUIREMENTS.**

The Ports and Waterways Safety Act (33 U.S.C. 1221 et seq.) is amended by adding at the end a new section 15 as follows:

"SEC. 15. TANK VESSEL INSURANCE REQUIREMENTS

"(a) INSURANCE REQUIREMENT. The person owning, operating, or demise chartering a tank vessel over 10,000 gross tons engaged in the foreign trade that is carrying oil in bulk as cargo or cargo residue shall maintain insurance, in accordance with regulations promulgated by the Secretary, to pay losses for oil pollution damage in the amount of up to $2,000,000,00 per occurrence if the vessel--

"(1) uses any place subject to the jurisdiction of the United States; or

"(2) uses the waters of the exclusive economic zone to transship or lighter oil destined for a place subject to the jurisdiction of the United States.

"(b) MANDATORY EXCESS INSURANCE FACILITY.

"(1) Charter. The Secretary shall charter a

private, not-for-profit, mutual insurance corporation to provide--

"(A) insurance required under this section; and

"(B) evidence of financial responsibility required under Sec. 1016(a) of the Oil Pollution Act of 1990 (33 U.S.C. 2716) and the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (42 U.S.C. 9601 et. seq.).

"(2) Name, Status, Authority and Purpose. Except as otherwise provided in this section, the corporation shall be--

"(A) known as the Mandatory Excess Insurance Facility;

"(B) a government-sponsored enterprise as defined in section 622(8) of title 2, United States Code;

"(C) subject to the District of Columbia Nonprofit Corporation Act and authorized to exercise the powers conferred upon a not-for-profit corporation by that Act; and

"(D) limited to the purposes set forth in this section.

"(c) **BOARD OF DIRECTORS.**

"(1) Composition. The board of directors shall

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consist of 9 individuals, 4 of whom are appointed by the Secretary and 5 of whom are elected by the policyholders. The appointed board members shall be 2 individuals from interested governmental departments and 2 individuals experienced in the maritime insurance industry. A majority of the board of directors shall be citizens of the United States.

"(2) Powers. The board shall--

"(A) be responsible for the management of the corporation;

"(B) establish, assess, and collect premiums only--

(i) on the basis of a vessel's tonnage; and

"(ii) on a per-voyage basis; and

"(C) adopt by-laws subject to the approval of the Secretary including provisions for the qualifications and terms of office of directors.

"(d) **CAPITALIZATION OF THE CORPORATION.**

"(1) Borrowing Authority.

"(A) Issuance of Obligations. The corporation may issue and sell bonds, notes, and other evidence of indebtedness (collectively referred to in this section as "bonds").

"(B) Not Obligations of the United States. Bonds issued by the corporation under this section

shall not be obligations of, or guaranteed as to principal or interest by, the United States, and the bonds shall so plainly state.

"(2) No Capital Stock or Dividends. The corporation shall not issue capital stock. No dividends shall be declared or paid to any holder of securities or insurance policies issued by the corporation.

"(e) APPLICABILITY OF OTHER LAWS.

"(1) Tax Laws. The corporation, including its capital, reserves, and surplus, and its income and property, shall be exempt from all taxation imposed by the United States or by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority.

"(2) Securities Laws. All bonds and stock issued by the corporation under this section shall be deemed to be exempt securities for the purposes of the laws administered by the Securities and Exchange Commission, to the same extent as securities which are direct obligations of, or obligations guaranteed as to principal and interest by the United States.

"(3) Banking Laws. The corporation shall be deemed to be an agency of the United States for the purposes of section 14(b)(2) of the Federal Reserve Act (12 U.S.C. 355).

Sec. 3. TRANSITION AND EFFECTIVE DATES.

(1) Not later than 180 days after the enactment of this Act, the Secretary of Transportation shall issue regulations with respect to the establishment, organization, management, and operation of the corporation established by this Act.

(2) Not later than 1 year after the enactment of this Act, the corporation established by this Act shall be operational.

(3) Not later than 2 years after the enactment of this Act, the corporation shall issue insurance required under section 15(a) of the Ports and Waterways Safety Act (as enacted by section 2 of this Act) unless extended for cause by the Secretary.

(4) Section 15(a) of the Ports and Waterways Safety Act (as enacted by section 2 of this Act) shall be effective on the date insurance is made available under Section 15(b) of that Act.

(5) Notwithstanding section 15(c) of the Ports and Waterways Safety Act (as enacted by section 2 of this Act), the initial board of directors shall consist of the 4 individuals appointed by the Secretary. Within one year after insurance policies are issued as required by paragraph (3) of this section, 5 additional directors shall be elected by the policyholders.

Hearing on the Coast Guard's

Interim Final Rule for

Vessel Certificates of Financial Responsibility

Statement of

W. Bruce Law

Executive Vice President

Allied Towing Corporation

representing

The American Waterways Operators

Before the Subcommittee on Coast Guard and Navigation

Committee on Merchant Marine and Fisheries

U.S. House of Representatives

July 21, 1994

Good morning, Chairman Tauzin and members of the Subcommittee. My name is Bruce Law, and I am Executive Vice President of Allied Towing Corporation, a Norfolk, Virginia-based transportation company operating 15 tank barges and seven tugboats. Allied is a family-owned company which has been in business since 1956. I am appearing here today on behalf of the American Waterways Operators (AWO), the national trade association representing the inland and coastal barge and towing industry. AWO's membership includes the owners and operators of tugboats, towboats, and barges, as well as the shipyards that build and service these vessels.

I would first like to express my appreciation to you, Mr. Chairman, for scheduling this hearing on the Coast Guard's interim final rule for vessel certificates of financial responsibility (COFRs) in such a timely manner. As you well know, given the severe financial, employment and operational disruptions which could result from the promulgation of unworkable COFR regulatory requirements, an often heated debate concerning implementation of this section of the Oil Pollution Act of 1990 (OPA 90) has gone on for nearly four years. Now that the interim final rule has been published, the "impasse" has been forcibly broken, and the speculative consequences which have been debated in the past will shortly give way to real, measurable financial impacts which may not only adversely affect marine companies like mine, but also the millions of Americans that rely on fuel sources dependent on waterborne commerce. We appreciate the opportunity to appear before you today to identify for the Subcommittee the impact of this rule on the U.S. towing industry. Our testimony this morning will focus specifically on the impact of the interim final rule on independent coastal tank barge operators. These are the companies -- like my own -- which stand to lose the most if the Coast Guard's financial responsibility rule is implemented as currently drafted.

Under the terms of the interim final rule, all tank barges which carry oil or hazardous substances in U.S. waters must obtain and carry a new COFR by July 1, 1995. The rule establishes five alternatives by which a vessel operator may demonstrate financial responsibility and obtain a certificate:

1. Insurance. Under this option, a vessel operator must file with the Coast Guard's National Pollution Funds Center an insurance guaranty form executed by not more than four insurers which have been accepted by the agency for purposes of providing financial responsibility guaranties under OPA 90;

2. Surety bond. Under this option, a vessel owner must obtain a surety bond guaranty executed by not more than four surety companies authorized by the U.S. Treasury Department to issue such bonds;

3. Financial guaranty. A vessel owner must file a financial guaranty form executed by not more than four financial guarantors who have been approved by the Coast Guard;

4. Self-insurance. To self-insure, a vessel owner must file financial statements demonstrating that the company maintains, in the United States, net worth and working capital equal to or greater than the total amount of financial responsibility required. Net worth is defined as U.S.-based assets less worldwide liabilities; working capital is defined as current assets located in the U.S., less current liabilities anywhere in the world. The rule provides that the Coast Guard may waive the working capital requirement if an applicant can demonstrate that working capital is not a significant factor in the company's financial condition; or,

5. Other evidence of financial responsibility. A vessel owner may also request that the Coast Guard accept a method of demonstrating financial responsibility other than one of the four options outlined above. However, the interim final rule makes clear that the proposed alternative may not be an alternative means of satisfying the self-insurance requirements of the rule, nor may it simply delete or alter a provision of one of the other acceptable methods.

The impact of these requirements on the tank barge industry is at best highly uncertain. At worst, it threatens the very existence of the small- to medium-sized coastal companies which

have long played a critical role in the distribution of petroleum products within the U.S. Perhaps the most pronounced concern of the tank barge industry with respect to the interim final rule is this: We face these threatening impacts not because the existing system of providing pollution liability coverage in this country has failed to function, but because the Coast Guard has failed to find a way to incorporate in the financial responsibility regulations a mechanism which allows this time-tested system to continue to function.

For years, many coastal tank barge operators have obtained pollution liability coverage through the International Group of Protection and Indemnity (P & I) Clubs. By all accounts, this system has worked extremely well: the P & I Clubs have a distinguished history of full and prompt payment of pollution liability claims for spills ranging in size from small to catastrophic. Recent major spills including the *World Prodigy, Presidente Rivera, American Trader, B. T. Nautilus, Mega Borg,* and *Sammi Superstars* incidents were all covered in full by the P & I Clubs.

Regrettably, however, instead of adopting a rule which builds upon this longstanding, well-tested and widely understood insurance system which supports the coastal tank barge sector, the Coast Guard would have vessel operators, who currently insure with P & I Clubs, stake their companies' futures on an entirely new regime, the success of which is based upon the potential viability of two new entities which are not yet in existence and thus have no proven business track record. Moreover, the much higher costs -- newly added costs -- associated with this new system provide absolutely no greater guarantee to the public that more secure funds will be available to clean up spills should they occur. Perversely, it appears that what the proposed system may actually do is encourage vessel operators to reduce the level of insurance coverage which they have historically carried, and instead obtain a guaranty of insurance sufficient only to meet the OPA-mandated liability limits -- ironically, at a potentially much higher rate. This would in fact reduce the financial ability of companies to clean up spills. It would also expose the Oil Spill Liability Trust Fund to a greater financial drain than would have occurred under existing marine insurance practices.

These general impacts resulting from the interim final rule are important matters of public policy of which the Subcommittee and the Congress should be aware, and I hope about which you are concerned. Unfortunately, as I view many congressional debates from "outside the beltway," the fact that otherwise unnecessary costs are added to business activities often appears to be at best a minor factor in whether a particular law is passed, particularly where environmental concerns are driving the debate. While it may be true that the major oil companies will be able to pay the higher costs resulting from these new COFR requirements, many smaller, independent companies like Allied will not. I simply cannot accept that it was Congress's intent to drive small, responsible companies like mine out of the oil and chemical transportation business.

With these general comments as a backdrop, I would now like to discuss some specific examples of the kinds of impacts which we expect will result if the interim final rule for COFRs is implemented as currently drafted. These real-world examples from the coastal barge and towing industry give meaning to the general results which we predict.

First, in the absence of a system which relies on traditional insurance mechanisms, the most logical alternative for a very large company is self-insurance. The self-insurance formula established in the interim final rule, however, is so stringent that even the most highly capitalized companies in the coastal towing industry cannot meet its provisions without obtaining a waiver of the working capital requirement. While this may in fact be possible -- the Coast Guard has indicated that it does intend to grant waivers in appropriate circumstances -- something is clearly wrong with a regulatory formula which even the largest and most financially stable companies in the industry cannot meet. In addition to granting waivers where appropriate, the Coast Guard should modify the self-insurance formula to incorporate in the regulations themselves reasonable criteria which allow financially stable companies with significant net worth to self-insure without having to rely on a potentially unpredictable waiver process.

Second, while self-insurance (provided that a waiver of the working capital requirement can be obtained) may be an option for the largest companies, it is not an option for a small- to medium-sized coastal company like mine. For Allied and companies like it, the only real alternative is to find an insurer willing to act as guarantor for purposes of the financial

responsibility requirements of OPA 90. However, because the insurers upon whom we now rely for pollution coverage have said that they cannot act in that capacity, we are faced with a significant -- and for some companies, an unbearable -- layer of additional costs.

Let me give you an example from my own company's experience. For the 1994-1995 policy year, Allied Towing will pay just under $1 million for liability coverage from our P & I Club. In addition to standard P & I coverage, that coverage includes oil pollution liability coverage up to $500 million per incident, plus $1 billion of coverage for any other type of incident, including a hazardous substance spill, for our entire fleet. Under the interim final rule, however, this coverage cannot be used to satisfy my company's COFR requirement of $10 million for oil pollution coverage and an additional $5 million for hazardous substance coverage. For that, we will have to obtain an insurance guaranty from Shoreline Mutual, assuming that entity obtains the necessary reinsurance and becomes viable. As of June 23, Shoreline advises me that a $10 million COFR covering my five oil tank barges only will cost $1,851,479 per year. The additional costs to provide $5 million dollars in coverage for Allied's ten tank barges in chemical service are still undetermined. This means that my insurance costs would more than double, while my level of insurance coverage would decrease to just one percent of its present level! Even if my company could afford this substantial increase in costs, this massive decrease in liability coverage is something which neither I nor my shipper-customers can accept. Operating oil and chemical barges with just $15 million of pollution coverage clearly endangers the viability of Allied Towing. It also exposes the Oil Spill Liability Trust Fund to a degree far in excess of its current level. This seems entirely at odds with the spirit and purpose of OPA 90.

Mr. Chairman, AWO and its members have supported enactment of comprehensive oil spill legislation since 1975. Considering the environment in which it was debated and enacted, we believed OPA 90 to offer a potentially manageable approach to oil spill prevention and response. That conclusion, however, was founded on the expectation that the Congress intended and supported the continuation of the marine transportation industry's role in petroleum transportation, under a time-tested insurance system which has heretofore worked exceptionally well. Whether the interim final rule permits the needed degree of flexibility required for a successful operational transition from the current system is unfortunately at this late date still very much in doubt.

The reality of the new financial responsibility regime is this: Large, well-capitalized coastal tank barge operators cannot feasibly comply with the self-insurance requirements of the interim final rule without a Coast Guard waiver. Smaller coastal companies will either be forced to absorb tremendous new costs or to exit the oil and chemical transportation business altogether. And for all of this, the assurance that the resources necessary to clean up a spill will be available will in no way be increased. Both the industry and the public deserve better.

I thank you again for holding this hearing and I will be happy to answer any questions you might have.

TESTIMONY OF

Miles A. Kulukundis,

Chairman

International Association of

Independent Tanker Owners

(INTERTANKO)

Before the

Subcommittee on Coast Guard and Navigation
Committee on Merchant Marine and Fisheries
U.S. House of Representatives

Oversight Hearing
Vessel Certificates of Financial Responsibility
Interim Final Rule

1334 Longworth House Office Building
July 21, 1994

TESTIMONY OF MILES A. KULUKUNDIS,
CHAIRMAN, INTERTANKO

On behalf of the International Association of Independent Tanker Owners (INTERTANKO), I thank you for the opportunity to appear before the subcommittee today. INTERTANKO is a non-profit association comprised of some 265 tanker companies in 36 maritime countries, including the United States. More than 50 percent of the world's tanker tonnage is entered in INTERTANKO.

Nearly three years ago, the Coast Guard issued a proposed rule to implement the financial responsibility provisions of the Oil Pollution Act of 1990 (OPA). In November 1991, my predecessor as Chairman of INTERTANKO, Mr. Andreas Ugland, appeared before this very subcommittee and explained the serious risks confronting shipowners and the United States if the Coast Guard implemented the rules as proposed. The problem which I wish to address today and which we addressed in 1991 is the inability of the marine insurance system to meet the requirements of this rule.

Despite the passage of a great deal of time and the contribution of significant resources on the part of the world maritime community, the interim final rule on vessel financial responsibility published by the Coast Guard on July 1st is little changed from the proposed rule that so concerned industry and this subcommittee in 1991. The interim final rule exposes the United States and those that serve its domestic and foreign trades to precisely the risks about which INTERTANKO and many others warned this subcommittee and the Coast Guard.

Under the interim final rule, the Coast Guard will accept any one or combination of the following methods of establishing financial responsibility: surety bonds, self-insurance, financial guaranties, insurance and "other evidence of financial responsibility." Because the Coast Guard has decided to implement the financial responsibility requirements of the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) along with those of OPA, most tankers are required to provide financial responsibility of $1,500 per gross registered ton. Tanker owners and operators must comply with the interim final rule by December 28th of this year.

What are the dangers that confront us? Perhaps the most immediate is that OPA, through the interim final rule, may act to deprive U.S. trades of a reliable, proven, cost-effective system for handling pollution claims. I am of course speaking of the P&I Club system.

P&I Clubs are not "insurers" in the traditional sense. P&I Clubs are not-for-profit, mutual risk associations composed of shipowners and operators. Through mutual indemnification and reinsurance, the P&I Clubs provide insurance coverage.

The record of the international system of P&I Clubs in handling both pollution and other maritime claims is exceptional. Through a complex and highly evolved structure of risk apportionment and reinsurance arrangements, coverage for each tanker in excess of $500 million has been secured at astonishingly low costs to vessel owners and operators. This provides a level of cover that exceeds the OPA requirements of $1,500 per gross registered ton by a factor of five or more for most tankers. The Clubs have a perfect record in compensating pollution claims and have never abandoned shipowners or claimants. American importers and exporters benefit from this cost effective system.

The P&I Clubs have also been the predominant provider of evidence of financial responsibility under the provisions of the Federal Water Pollution Control Act

(FWPCA). Currently, the 18 members of the International Group of P&I Clubs provide over two-thirds of the guaranties needed to obtain FWPCA COFRs.

Almost from the day of enactment of OPA, the P&I Clubs have stated that direct action, the lack of policy defenses, and the potential scope of damages under OPA, as well as serious concerns over state laws, force them to conclude that it would be imprudent for Clubs to provide evidence of financial responsibility under the OPA system. The witnesses for the Clubs can and will explain their position better than we. What prompts comment are assertions that the P&I Clubs' position can be transformed simply by shipowners directing the Clubs to do so.

While the P&I Clubs are composed of shipowners and are governed by Boards of Directors of shipowners, it must be understood that the substantial majority of Club members are not trading to the United States. Furthermore, the majority of the members are not tanker owners. Shipowners who participate in the global system of marine insurance provided by the Clubs do not want the integrity of that system to be put at risk by OPA guaranty provisions. The Coast Guard is simply wrong in assuming that the Clubs are "captives" of tanker owners who trade to the United States. The issue is obviously far more complex and diffuse than the Coast Guard acknowledges.

Although the Coast Guard strongly suggests that the COFR problem can be avoided by a few words from tanker owners to their Clubs, the Coast Guard has placed great faith in the appearance of "alternative" evidence of financial responsibility. As tanker owners confronted with the potential loss of their traditional sources of guaranties in the U.S. market, we would certainly like to share the Coast Guard's optimism. Indeed, several of the entities identified by the Coast Guard as alternatives have devoted a great deal of thought and effort to finding viable ways of meeting OPA's requirements. Many shipowners may have to turn to these new providers if they are to continue to trade to the United States.

Nothing I say should in any way be interpreted as criticism of these alternative plans. Rather, I am trying to describe to you the concerns tanker owners have during the quickly diminishing period between now and December 28, 1994. One of the problems for a tanker owner contemplating use of these new methods is that, from information available at this time, shipowners may have access to considerably less coverage at substantially increased costs. These concerns are confirmed by information in the record of the Coast Guard's rulemaking. The Coast Guard itself reckons that the costs of alternative forms of guaranties may be seven times the present level.

The Coast Guard trivializes the impact of the potential costs by stating they will cause only a minor rise in the cost of gasoline at the pump. The point is not what the COFR program costs at the pump. The point is whether vessel owners should be forced to incur significant increased costs that serve no purpose other than to meet the structural requirements of OPA and the IFR. These costs are substantial to a shipowner and will be taken into consideration when making his trading decisions.

The problem is not confined to the cost side. The record before the Coast Guard, as well as descriptions of the alternative plans provided by their promoters, indicates that alternative plans for certificates will provide financial responsibility only for the statutorily required level. Owners now obtain evidence of financial responsibility from the P&I Clubs as part of their $500 million in pollution coverage. These owners may find themselves required to have separate insurance for the sole purpose of obtaining COFRs in amounts up to $300 million for a VLCC. These COFR

requirements are quite independent of whatever insurance level the shipowner must maintain and may well conflict with existing Club and reinsurance facilities.

This scenario is aggravated by the untried, unknown and unforeseeable nature of these new purpose-built entities. If claims are asserted against them, will they have the experience, resources and skills necessary to process smoothly the claims and to deal with the other complex daily tasks essential to an adequate spill response? Do we know whether these alternative providers will be able to sustain multiple incidents in quick succession?

The current P&I Club system is excellent in these aspects and has a century-long track record. At a time when we are all operating under a heightened concern for rapid response to environmental mishaps, are we prepared to forego the experience, knowledge, and skilled personnel provided by the P&I Clubs?

The liability concerns highlighted by the P&I Clubs' position on the interim final rule are but a component of a dilemma facing all shipowners who trade to the United States. Under the IFR, will a shipowner be able to find ample levels of protection at a reasonable cost from providers whose operational histories instill confidence?

On the basis of information currently available, the vast majority of independent tanker owners and operators will be unable to comply with the new regulations. Of the methods for establishing evidence of financial responsibility mentioned in the IFR, none will be universally available at reasonable cost to the tanker fleet serving the United States. Only the most highly capitalized or domestically based owners can meet the self-insurance or surety options. None of the alternative insurance providers have been deemed "acceptable" by the Coast Guard.

Every tanker owner, therefore, faces a severe dilemma. As we sit here today, for the average independent tanker owner, there is no known means for complying with the interim final rule. Each individual owner will have to wrestle with this issue in the coming months. But every tanker owner's problem is a problem for the United States as well. The IFR has subjected the flow of petroleum to requirements for which there are no present solutions.

INTERTANKO pledges to work with your subcommittee, the Coast Guard, cargo owners, the P&I Clubs, and the proposed alternative providers of financial responsibility to endeavor to comply with the new regulations. We will examine every methodology and proposed scheme to try to find ways to maintain service and protection at high levels. We will continue to support the Mandatory Excess Insurance Facility (MEIF) put forward by the Greek, Norwegian and Swedish shipowner associations as a method of solving both the liability and COFR concerns raised by OPA.

INTERTANKO believes that any solution should be based on the existing P&I Club system. As already stated, the P&I Clubs have been the reason why the industry has been able to provide quick, dependable and substantial funds to pay oil spill response costs and damages.

As a departing thought, we must appeal to the members of this subcommittee that they be prepared to revisit this issue if no viable alternative emerges. In that event, we must look to you for guidance, assistance and leadership.

Thank you for the opportunity to present this testimony. I will be pleased to answer any questions.

TESTIMONY OF

THE NATURAL RESOURCES DEFENSE COUNCIL
OCEAN ADVOCATES

ON THE COAST GUARD'S INTERIM FINAL RULE

FOR VESSEL CERTIFICATES OF FINANCIAL RESPONSIBILITY

BEFORE THE

COAST GUARD AND NAVIGATION SUBCOMMITTEE

COMMITTEE ON MERCHANT MARINE AND FISHERIES

U.S. HOUSE OF REPRESENTATIVES

JULY 21, 1994

Prepared by:

Lisa Speer
Senior Policy Analyst
NRDC

Mr. Chairman and Members of the Committee:

My name is Lisa Speer. I am senior policy analyst with the Natural Resources Defense Council (NRDC), NRDC is a national environmental organization has a long history of involvement in the enactment and subsequent implementation of the Oil Pollution Act of 1990 (OPA). My testimony today is on behalf of NRDC and Ocean Advocates.

We have done an preliminary review of the Coast Guard's interim final rule implementing OPA's financial responsibility provisions (Section 1016 of the Act), and will be reviewing the rule and the Regulatory Impact Statement (which we have not received as of this writing) in more depth over the next two months as we prepare comments for the September 29th deadline.[1] Based on our preliminary review, we support the Coast Guard's overall approach.

The importance of financial responsibility rules

Enacted in the wake of the Exxon Valdez disaster, OPA contains a broad range of measures designed to improve the safety of oil transportation in the United States. At the heart of OPA is the principle that the polluter should pay promptly for cleanup and damages caused by spills. This "polluter pays" principle rests on both the statutory liability limits and the requirement that owners and operators demonstrate that they have the financial wherewithal to pay for a spill up to those limits. By ensuring that a potential spiller can pay for cleanup and damages up to OPA's liability limits, financial responsibility requirements provide strong financial incentives to prevent spills and help discourage "fly-by-night" operators. They also ensure that the spiller, and not the taxpayer, pays the costs of spills.

Prompt implementation of these rules is important because certain pre-existing financial responsibility regulations will remain in effect until the new rules go into effect. Since existing regulations ensure financial responsibility at levels generally far lower than those required by OPA, claimants could fail to obtain OPA levels of compensation from a spiller. For example, under the new rules, vessel owners will be required to provide evidence of financial responsibility of $1200 per gross ton, depending on the type of vessel. Under existing financial responsibility requirements in the Clean Water Act, vessel owners are required to provide evidence of financial responsibility of only $150 per gross ton. That amount of financial responsibility could be wiped out very quickly even in a relatively small spill.

The roughly 750,000 gallon spill from an oil-laden barge off Puerto Rico earlier this year illustrates this point. The barge operator's OPA liability amounted to some $10 million, but under the existing financial responsibility requirements in the Clean Water Act, its insurer had provided a guarantee of only $800,000. While the insurer has agreed to pay the full $10 million, it was not obligated to do so. A less responsible insurer might not be as obliging.

Industry objections

The industry has raised a number of arguments against the financial responsibility rules, most of which have little to do with the specifics of the rule. Instead, the industry has used

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[1] This testimony does not address several new issues raised in the interim final rule, including new provisions on joint and several liability for co-subscribing guarantors, the "other evidence" provision, and other new issues because we have not had the opportunity to review the Regulatory Impact Analysis accompanying the rule.

the rulemaking as a forum to express its opposition to certain provisions of OPA, most notably those providing for "direct action" against guarantors, the absence of state pre-emption, and the fact that OPA's liability limits are higher and more easily broken for owners and operators (but not, notably, for guarantors) than those under the existing international regime.

The provisions of OPA that industry objects to were enacted unanimously by the Congress in 1990 for good reason. For example, all pre-OPA pollution laws leave intact all state oil spill liability and compensation laws. These laws allow a state to proceed against a spiller to recoup costs and damages incurred by the state resulting from a spill.

With respect to direct action, under which claimants may bring an action directly against a guarantor for costs and damages arising under OPA, this feature of OPA is essential to ensure that the U.S. taxpayer does not end up paying the costs of oil spills. Financial responsibility provided by a guarantor without an underlying right of direct action against that guarantor is not an enforceable assurance of financial responsibility. For this reason, the Clean Water Act, the Trans-Alaska Pipeline Authorization Act, the Outer Continental Shelf Lands Act all contain direct action provisions in some form as do the laws of at least 79 other countries, according to the Coast Guard.

With respect to the liability limits in OPA, there is evidence that they are too low, not too high. In the Puerto Rico barge spill, for example, clean up costs reportedly topped $20 million -- twice the OPA liability limit for the vessel[2] and twenty-five times the COFR amount required under the Clean Water Act, in the first ten days of the spill. Clean up costs and damage claims (not including damages to natural resources, which have yet to be assessed) now stand at roughly $100 million. The consumer, through the Oil Spill Liability Trust Fund, will thus end up paying the vast majority of the cost of that spill.

Some have argued that direct action, combined with no state-pre-emption and more breachable liability limits, mean that guarantors face unlimited liability under OPA. This is clearly and unequivocally wrong. The statutory limits on liability under OPA 90 are clear and specific, as is the provision that a guarantor's liability cannot exceed these limits. This is true even if in a particular case the limits are not applicable to the insured responsible party (because of gross negligence, for example). The Coast Guard's final rule restates this principle.

Membership in P&I Clubs as an asset

Some have proposed that membership in a P&I Club should be treated as an asset, thus allowing the vessel owner to self-insure. This approach would completely undermine the spiller pays principle because the P&I Clubs could invoke an unlimited number of policy defenses, such as bankruptcy, that would result in non-payment by the Clubs. Allowing such policy defenses to invalidate insurance coverage would be in clear contravention of the direct action requirement of OPA 90 and the principle of full compensation. It was properly rejected by the Coast Guard.

The "train wreck"

Various dire warnings have been sounded from various quarters about the impact of the Coast Guard's rule. Under the "train wreck" scenario, the P&I Clubs will continue to refuse to act as guarantors, no other options will be available to vessel owners, vessels will stop delivering oil to the United States and the economy will collapse. This scenario is not credible for the following reasons.

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[2] This assumes the barge owner's OPA liability limit is not broken.

First, the P&I Clubs are controlled by their member shipowners and operators, who elect the Clubs' Directors and appoint the Club's managers. The notion that vessel owners and operators are powerless to influence the position of the Clubs is not credible.

Second, similarly dire predictions were made during the debate over OPA that vessels would stop serving US ports as a result of the greater oil pollution liability placed on them by OPA. According to a study by DOE cited by the Coast Guard, these threats were largely empty; virtually all independent tanker companies remain in the U.S. tanker market, and the vast majority of oil companies are committed to maintain or expand their fleets.

Third, US trade accounts for approximately one third of all world seaborne oil movements. The likelihood that major oil companies and independent tanker owners would simply abandon the US market rather than order the P&I Clubs to revise their policy is similarly not credible.

Finally, as testimony of previous witnesses has indicated, alternative financial responsibility sources are available. These alternatives include commercial insurance entities and surety bond companies, as well as the potential greater use of self-insurance and financial guaranties.

Conclusion

The unfolding Exxon-Valdez trial serves as a grim reminder of the enormous environmental, economic and social costs of oil spills. Effective financial responsibility rules help provide a powerful incentive to companies not to spill, and ensure that the wherewithal to clean up and restore damaged resources is paid for by those that profit from the transportation of oil.

The Coast Guard's overall approach is legally sound, fiscally prudent, ecologically appropriate, and long overdue.
We strongly support the Coast Guard's general approach in the final rule, and believe it represents a major step toward improving tanker safety.
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July 20, 1994

The Honorable W. J. (Billy) Tauzin
Chairman
Subcommittee on Coast Guard and Navigation
House Merchant Marine and Fisheries Committee
541 Ford House Office Building
Washington, D.C. 20515-6230

Dear Mr. Chairman:

We have noted, with interest, press reports on Hearings of the Subcommittee on Coast Guard and Navigation scheduled for July 21, 1994 relative to the Coast Guard's Interim Rules for Certificates of Financial Responsibility under the Oil Pollution Act of 1990 ("OPA '90"). We write to inform the Subcommittee of the status of the development of "First Line" as a potential guarantor of financial responsibility under OPA '90 and the Interim Rules.

"First Line" is a joint project of insurance brokers Johnson & Higgins and Nicholson Leslie BankAssure. Headquartered in New York City, Johnson & Higgins is one of the world's largest international brokers and has an extensive Marine and Energy clientele. J&H has been both directly and indirectly involved in the formation of several insurance companies. Also, we are by far the world's largest manager of captive insurance companies. J&H has extensive experience handling P&I and pollution insurance.

Lloyd's broker Nicholson Leslie BankAssure is a subsidiary of the Nicholson Leslie Group. BankAssure specializes in handling insurance for major banks and financial institutions financing shipping and airline companies. In recent years BankAssure has focused on vessel pollution and have originated and developed specialized insurance products for their banking clients. They are the leading brokers in this field.

Our firms are currently in the process of finalizing plans looking towards the raising of capital and the arrangement of reinsurance to enable "First Line" to qualify with the Coast Guard as a guarantor. Although J&H and BankAssure have been working on the "First Line" concept since the passage of OPA '90, this process can be initiated in earnest only after the publication of the Interim Final Rule and the establishment of an implementation schedule for Certificates of Financial Responsibility.

Our efforts have intensified since July 1st and our activity is the product of over two years of development and research. Commercial providers of financial guarantees for shipowners became necessary only after Congress enacted OPA '90, which was largely in response to the EXXON VALDEZ oil spill, and was the culmination of previous unilateral pollution legislation by the U.S.

We have endorsed the position taken by many international shipping organizations, as well as by many in the United States, namely that the international regime of the Civil Liability and Fund Convention, in effect since 1969, and currently in force in 57 countries, is best suited for dealing with oil pollution. Accordingly, we have eschewed public statements of support for the COFR regime established by OPA '90 and, indeed, have supported and continue to support efforts within the shipping community to achieve an international solution for the United States.

The traditional providers of both pollution insurance and "Evidence of Financial Responsibility" are the shipowners' Protection & Indemnity Associations or P&I Clubs. The Clubs have stated repeatedly that they are prepared to continue providing pollution insurance for their members' ships while in U.S. waters, and "Evidence of Financial Responsibility", but they cannot assume, as guarantors, all the conditions and exposures contemplated by the Rules as finally adopted.

Unfortunately, the Coast Guard has not been able to offer a compromise to the Clubs that would allow them to continue to provide Evidence of Financial Responsibility as in the past. Consequently, shipowners and operators need a new insurance product that meets the requirements of OPA and the Interim Rule and that keeps shipowners' costs to a minimum. This is the purpose of the "First Line" effort. Johnson & Higgins and BankAssure intend to continue efforts to bring the "First Line" concept to fruition and hence available to shipowners and operators under the law as currently enacted.

As insurance brokers, our mission is to assist our clients in analyzing and assessing their risk management needs and, where appropriate, to negotiate sound, economical insurance solutions on their behalf. From time to time, suitable insurance products are not available to our clients and in such circumstances we will seek to arrange for new insurance facilities and products.

Relative to OPA '90 issues, we believe it important to present shipowners and operators with a means to comply with statutory and regulatory requirements through

Johnson & Higgins

The Honorable Billy Tauzin
Chairman
July 20, 1994
Page 3

a financially sound enterprise dedicated to the provision of a reasonably priced insurance product that will complement existing market resources. This, perhaps, is a perspective that may be somewhat different from that of the participants at your Hearing or those who have submitted comments to the Coast Guard.

We thank you for this opportunity to provide our views to the Subcommittee and we request that this letter be incorporated in the record of the Hearing.

Sincerely,

Micheel J. Northmore
Vice President

D. Darby Duryea
Managing Principal and
Senior Vice President

Graham D.R.D. Barnes
Chairman - Nicholson
Leslie BankAssure,Ltd

MN/di

TESTIMONY OF
JERRY A. ASPLAND
PRESIDENT, ARCO MARINE, INC.
and
CHAIRMAN, API GENERAL COMMITTEE ON MARINE TRANSPORTATION
BEFORE THE SUBCOMMITTEE ON COAST GUARD AND NAVIGATION,
HOUSE COMMITTEE ON MERCHANT MARINE AND FISHERIES
ON
FINANCIAL RESPONSIBILITY FOR WATER POLLUTION (VESSELS)
JULY 21, 1994

Good Morning, Mr. Chairman and Members of the Subcommittee. My name is Jerry Aspland, I am President of ARCO Marine, Inc. and Chairman of the American Petroleum Institute's (API) General Committee on Marine Transportation. API represents over 300 companies involved in all aspects of the oil and gas industry, including exploration, production, transportation, refining and marketing. API member companies and their marine affiliates transport large volumes of petroleum and petroleum products into and within the United States, as well as own and operate sizable tanker and tank barge fleets under both U.S. and foreign registry. API member companies also charter a significant portion of the world's independent tanker and tank barge tonnage responsible for carrying the bulk of the imported oil that makes up approximately half of the United States petroleum consumption. Consequently, API is deeply concerned by the recently published Coast Guard Interim Final Rule (IFR) entitled "Financial Responsibility for Water Pollution Vessels", (CGD 91-005), 59 FR 34210 and have two requests. First, we respectfully request the Committee to seek monthly reports from the Coast Guard regarding the ability of the affected community to file approvable financial responsibility applications. Second, if circumstances do not develop as envisioned by the Coast Guard, we request this Committee to petition the Coast Guard to supplement the rulemaking to allow for more flexibility and compliance options.

As a representative of the seafaring segment of the petroleum industry that makes its living at sea, I am here today on behalf of men and women who have a deep and abiding respect for the marine environment. We strongly support the goals of OPA'90 to reduce the risks of oil spills and to provide a rapid and effective means of responding to an oil spill. We also recognize that a critical component of this goal is ensuring that vessel owners and operators have the financial means available to meet potential liabilities which may arise after a spill. API continues to endorse the principles enunciated by the Coast Guard that the polluter pays and that funds should be available without legal action. Nonetheless, the subject of this hearing is not an environmental issue it is a technical insurance issue.

We should make clear also that API regards the Coast Guard as a highly sophisticated and dedicated agency. Our often contentious disagreement with the Coast Guard on the Certificate of Financial Responsibility (COFR) rulemaking in no way diminishes our respect and regard. However, because API's principal commitment is to the efficient and dependable supply of petroleum products to U.S. consumers, we feel obligated to state that the Coast Guard has been exceedingly narrow in its selection of the commercial alternatives of financial responsibility which are available under OPA'90, and we believe that the IFR has the potential to disrupt the flow of oil to the U.S. industry and place whole segments of the United States economy at risk. We also believe that the Coast Guard's rule would result in higher premia than current P&I insurance without commensurate benefits; that OPA'90 allows the Coast Guard to promulgate regulation that would enable vessel owners to meet the Act's financial responsibility requirements utilizing their P&I insurance; that independent shipping firms that have high quality operations but cannot afford a COFR will likely leave the U.S. trade or go out of business; and, that it is uncertain whether the specialty insurance groups envisioned by the Coast Guard will emerge as planned.

Congress clearly demonstrated its intention to provide flexibility and discretion to responsible parties in evidencing the increased financial responsibility called for by OPA'90. The law explicitly provides that the financial responsibility requirements may be established by any one, or by any combination of six methods which the Secretary of Transportation determines to be acceptable. The Explanatory Statement of the OPA'90 Conference Committee noted that the Secretary of Transportation's authority in this regard was "....to foster a continuing market for providers of financial responsibility." Despite this guidance, the Coast Guard's rule effectively prevents vessel owners from using the established and financially sound international Protection and Indemnity (P&I) Club system to satisfy financial responsibility requirements under OPA'90. This system provides for 97 percent of all certificates presently issued to tank vessels by the Coast Guard.

The Coast Guard's Interim Final Rule.

Despite hundreds of comments from shipping groups urging flexibility, the IFR essentially mirrors the Coast Guard's proposed rule. The only means for demonstrating financial responsibility are insurance, surety bonds, guaranties or self-insurance. The basic components of each of these are unchanged. A new "other evidence" option allows for approval by the Coast Guard of a specialized letter of credit or some other commercially uncommon form of evidence. In all cases, except self-insurance, evidence providers will be considered guarantors.

Many oil companies and their marine affiliates may be able to meet self-insurance requirements for their own fleets if the Coast Guard grants a waiver of the working capital requirements. Some large U.S.-based independent vessel owners also appear to possess enough financial strength either to self-insure or utilize a surety bond. As a result, these companies, which represent only about one-third of the tanker owners who will require a COFR may gain a distinct cost and strategic market advantage over less highly capitalized though high-quality operators. Without the ability to use P&I insurance, it is unclear to API how the remaining two-thirds of tanker capacity will be able to provide sufficient evidence of financial responsibility to enable them to continue operations in U.S. waters.

The Coast Guard Regulatory Impact Analysis (RIA).

In the Regulatory Impact Analysis (RIA) accompanying the Coast Guard's rule, the agency distorts the influence API members have with P&I Clubs and attempts to preemptively deflect responsibility for the rule. For example, at Page 56, the Coast Guard states that "[a]ny severe economic disruption that would ensue because of a disruption in vessel operations appears to be remote, and is fully within the control of the international shipping community." The Coast Guard argues that because P&I Clubs are comprised of shipowners and operators, who elect the Club's directors and support the Club's managers, that they, therefore, ultimately control the P&I Clubs decisions. In reality, the Coast Guard knows that the international shipping industry is a highly diverse community composed of not only tanker owners, but also owners of container ships, cruise ships, car carriers, tug and barge fleets and others. It is precisely the diversity of the P&I Clubs' membership that prohibits them from acting cohesively on problems as complex as answering to pollution liability claims in U.S. courts. This is especially so considering that only a minority actually need the coverage required by OPA'90. The influence of this minority, of which API membership is a part, is diminished further when considering that participants in the U.S. trade generate only 15 percent of the P&I Club premia, but are responsible for 60 percent of the claims.

API respectfully submits that it is the Coast Guard that is in the best position to monitor the validity of the assumptions regarding the availability of COFR guarantors. The United States government acting through the Coast Guard, not the international shipping industry, has the means and responsibility to ensure that the economy and the members of the American society are neither damaged nor needlessly inconvenienced by this rule.

Specialty Insurance.

The Coast Guard is relying on the emergence of two new Bermuda-based specialty insurers who, according to the Regulatory Impact Analysis, will "step into the shoes of the P&I Clubs and offer insurance guaranties under the proposed COFR rules."

Conceptually, API does not in any way oppose the development of specialty insurers, yet we believe that there is still enormous uncertainty regarding their economic viability. Both facilities named by the Coast Guard exist only in the most incipient stages of development. It is revealing that the language used by the Coast Guard in the IFR and RIA to tout these companies is almost entirely in the future tense. API is unaware that either of these companies has any members. This may be because they are novel and untested. In any case, it is very uncertain whether there is sufficient reinsurance in the world's markets to accommodate insurers who would appear to be holding a relatively high concentration of risk. Recent catastrophes have sent Lloyd's into a prolonged cycle of contraction which has forced the insurance industry to begin searching unsuccessfully for untapped capacity. API members question if reinsurance is available for these specialty companies. If it is, why haven't reputable reinsurers come forward publicly to confirm such availability?

Given these unknowns, it is disturbing that the Coast Guard, to date, has chosen not to air for public comment the criteria it has established for judging these specialty insurers to be "acceptable." Assuming these criteria exist, a large disparity exists in the IFR by virtue of the Coast Guard's requirement that a new specialty insurer need only provide up to $300 million in coverage for the bulk of the industry it insures. This is in contrast to requirements that a well-established multinational corporation which is required to provide cumulative guaranties far in excess of this amount for the vessels it charters.

An additional problem is that specialty insurance is very costly. Rating quotations, to date, indicate they are six to nine times more expensive than the P&I surcharge on vessels making U.S. voyages. The Coast Guard RIA estimates a figure of $415 million dollars in premia per year. Assuming specialty insurers emerge as planned, owners of largely smaller independent tanker fleets, who may have no choice but to enroll in them, would be placed at a competitive cost disadvantage. When considering that vessel owners will, out of necessity, continue to carry P&I insurance, there appears to be a fundamental inequity in requiring smaller independent companies to pay hundreds of millions of dollars to entities which, simply represent a means for meeting Coast Guard COFR requirements.
This represents an extremely inefficient use of scarce capital and ultimately an unnecessary charge to U.S. consumers.

P&I Insurance.

Theoretically, the polluter pays principle, if correctly applied, provides some incentive for vessel owners to incur costs to reduce the chance of an oil spill. The Coast Guard has insisted that these costs be "internalized." Yet, the average sized vessel owner cannot internalize potential costs as high as $250 million let alone actually pay these costs should an oil pollution incident occur. These companies must externalize these potential costs by using insurance which offers broad-based low cost coverage.

P&I Clubs offer coverage far in excess of OPA'90 limits and, in fact, are contractually obligated to indemnify the vessel owner if he breaks the limits of liability up to the policy limits of $500 million, or $700 million where excess coverage has been obtained. Under this mutualization and reinsurance scheme, the major portion of the oil spill liability risk is spread internationally through premia or "calls" on all Club members. Another portion is concentrated in the United States through a "per call" surcharge. P&I Clubs share their risk with the $14 billion Lloyd's market.

Over the past ten years, P&I Clubs have had an impeccable record of paying for oil spill response and clean-up costs. While the Clubs have indicated that they are not interested in insuring the additional risks associated with being guarantors under OPA'90, API, from

the beginning has maintained that Congress gave the Coast Guard significant discretion to write a COFR rule which would allow vessel owners to utilize their P&I coverage. The dilemma created by the interim final rule could be avoided if P&I Club entry were considered in determining a vessel owner's status as a self-insurer.

It has been a primary mission of API's General Committee on Marine Transportation to identify and develop solutions that would allow the majority of the shipping community to comply with the Coast Guard's rule. API has endorsed and submitted to the docket options such as utilizing P&I Club coverage as an asset for self-insurance purposes and the assignment of right-of-claim. Because P&I insurance is the now most efficient, broad-based method for proving compliance with financial responsibility requirements, API is committed to continue to work with the Coast Guard and the P&I Clubs to find a methodology which will be amenable to both groups, and allow the industry to use this insurance.

Impacts of the IFR.

Absent being able to use P&I insurance, API currently sees no other workable insurance vehicle in the marketplace that will allow all vessel owners to compete on a level playing field. As stated earlier, it is unclear how the bulk of the international shipping industry, which is composed of smaller, independent tanker owners, will meet the requirements of the rule. As an organization whose member companies charter a significant percentage of such tonnage, we are very concerned.

There may be a restructuring of the shipping industry as companies vie for means to meet the requirements. Companies with a competitive advantage may take over or replace disadvantaged companies. Firms which run high quality operations but which cannot afford a COFR may leave the United States trade or go out of business.

Many independent refiners who do not operate vessels, may be forced to issue a separate guaranty for each vessel placed under charter implying a required guaranty capacity of up to several hundred million dollars per company -- an impossible situation.

In addition, a significant amount of oil, which is shipped to the United States, is traded while it is being transported on the open water. It is unclear how these trades will be impacted.

Conclusion.

The Coast Guard's implementation of the financial responsibility requirements of OPA'90 is poised to run afoul of commercial reality. The primary forms of financial responsibility allowed in the regulation are available only to a narrow segment of the industry. The only option left to the remainder of the industry are two Bermuda-based companies whose viability is not yet established. We cannot contemplate that Congress or the Federal Government would disrupt maritime commerce or cause other injury to the U.S. economy just to test the validity of the Coast Guard's assumption regarding their rule.

As citizens, we question the cost and benefits of the rule. With the P&I system providing $500 million in coverage coupled with their impeccable history of backing their insureds, this rule adds no value in term of insurance protection; it merely assures that some entity will be available to be sued by claimants. And, for this the American consumer will be asked to pay $415 million in additional insurance costs.

If the specialty insurance facilities do not emerge as anticipated by the Coast Guard, action must be taken to ensure that petroleum supplies are not interrupted. The variables which could lead to a potential disruption in oil supply, could materialize much more rapidly than the six-month compliance deadline contained in the IFR. Spot charters are fixed about 10 weeks in advance of a vessel's arrival in the U.S. and time charters take as long as four months to arrange. API urges this Committee and the U.S. Coast Guard to closely monitor the progress of industry toward compliance with this rule as quick, decisive action may be

needed to forestall the kinds of negative economic consequences foreseen for the Coast Guard in its RIA. Again, we hope the Chairman will monitor this situation very closely. We would like to be able to call on the Chairman, members of his staff and the influence of this Committee to make sure this situation is maintained under control.

API is ready and willing to cooperate and lend its resources and expertise toward reaching a prompt and effective solution to the financial concerns surrounding the costs of mitigating an oil spill. We are developing comments on the IFR which will hopefully present the Coast Guard with more options in developing its regulation. We will submit copies of our comments to you, Mr. Chairman, when they become available.

Thank you for the opportunity to testify today. I am prepared to answer any questions you may have.

AMERICAN INSTITUTE OF MERCHANT SHIPPING

Industry Advocate for 25 Years

Est. 1968

August 2, 1994

The Honorable W.J. (Billy) Tauzin
Chairman
Coast Guard and Navigation Subcommittee
House Merchant Marine and Fisheries Committee
541 Ford House Office Building
Washington, D.C. 20515

Dear Mr. Chairman:

The American Institute of Merchant Shipping (AIMS) is a national trade association representing 23 U.S.-flag carriers which own or operate approximately eleven million deadweight tons of tankers, dry bulk carriers, containerships, and other oceangoing vessels engaged in the domestic and international trades of the United States. AIMS represents a majority of U.S.-flag tanker and liner tonnage.

Our organization did not appear as a witness at the July 21, 1994 Subcommittee hearing on the Certificates of Financial Responsibility (COFR) issue. We would, however, request that this letter be made part of the July 21 hearing record. Since the closing date for comments on the Interim Final Rule (IFR) is September 29, 1994, these comments are preliminary in nature.

This controversy has been on-going since the Coast Guard published its Notice of Proposed Rulemaking (NPRM) in the September 26, 1991 Federal Register (56 FR 49006). AIMS submitted testimony for the record of the November 6, 1991 Coast Guard Subcommittee hearing and extensive comments to the NPRM docket on January 17, 1992, in which we argued, basically, that the Coast Guard had sufficient flexibility under the statute (OPA 90) to resolve the COFR problem administratively in the regulatory process and to consider membership in the P&I Clubs as evidence of financial responsibility so that COFRs could be issued and avoid the "guarantor" and "direct action" against the P&I Clubs pitfall. The Coast Guard published a Preliminary Regulatory Impact Analysis (PRIA) in the July 12, 1993 Federal Register (58 FR 38993), which was nothing more than a restatement of the arguments raised in the NPRM. The PRIA properly should have been prepared prior to the publication of the NPRM. On July 1, 1994 the Coast Guard announced the availability of the final Regulatory Impact Analysis (RIA) which was dated "June 1994." The RIA is substantially similar to the PRIA.

After an approximate four year period in which the Coast Guard received an overwhelming number of statements for the docket in opposition to the NPRM, the Coast Guard finally published in the July 1, 1994 Federal Register (59 FR 34210) its Interim

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Final Rule (IFR) which was basically the original unacceptable NPRM, with a schedule of compliance.

Since 1991 the Coast Guard in its NPRM and IFR has persistently refused to exercise its flexibility under the statute to make full use of the provisions in Section 1016(e) of the Act whereby the Coast Guard is empowered to accept "evidence of insurance, surety bond, guarantee, letter of credit, qualifications as a self-insurer or other evidence of financial responsibility" so as to permit the P&I Clubs to stand behind the necessary COFR. Instead the Coast Guard has persisted in placing total reliance on new untried and untested commercial insurance facilities such as Shoreline and Firstline to justify their approach to their COFR predicament.

The vast majority of shipowners will have to rely on insurance to demonstrate financial responsibility. Unfortunately, under the Coast Guard's IFR the only acceptable insurance appears to be these new entities of unknown characteristics, unknown security and unknown capabilities, all at substantially increased costs. The Coast Guard's course of action provides no advantage over the existing system which has performed so well for so many years. Indeed, the Coast Guard can produce no evidence to date that these new entities will work.

Since the Coast Guard is attempting to force a new uncertain market into existence through its restrictive rulemakings, the Coast Guard has the responsibility to oversee the ability or inability of the shipowning community to comply with its rule at reasonable costs and the subsequent impact on U.S. trade if they can't. The burden is on the Coast Guard.

Even if the new facilities do emerge, when considering the broad range of vessels in the U.S.-flag fleet and foreign-flag vessels serving the U.S. petroleum trades, the IFR has established an uneven playing field because some companies will be exposed to additional costs of obtaining this new COFR insurance that others will not have to bear. Some companies will be able to comply and others will not. But even those few who can comply will be exposed to additional costs to do so. Most companies will not be able to comply without a viable insurance facility emerging to take care of them. In place of the P&I Club system which has been reliable and equitable over the years, the Coast Guard in its intransigence is forcing on the carriers an unfair system of unequal costs. A few of our members will be able to self-insure and comply, but most of our members lack the financial wherewithal to comply.

In this same vein it must be recognized that an organization such as AIMS represents a variety of interests, not just tankers, and the IFR will affect them all in different ways. The AIMS membership consists of members that operate tankers (proprietary and independent), barges, container vessels, and so-called fast sealift and prepositioned RO/RO vessels on charter to the Military Sealift Command (MSC). Obviously a mix of vessels as diverse as that of the AIMS membership will all be impacted in different ways by this uneven IFR. The Coast Guard's schedule of compliance in the IFR clearly illustrates the uneven effect of this rule on the different types of vessels and operators within our membership.

By its own admission the Coast Guard has made no effort over the past four years to analyze the financial impact on the U.S. economy in the event of total or near total disruption of the U.S. petroleum delivery system. Instead they take refuge in such things as the absurdly low figure of $415 million quoted by the Coast Guard as the additional insurance costs to be borne by the industry and the excessive trust they have placed in

untested commercial solutions which will substantially raise costs to the vessel operators and thus to the United States.

We agree with the American Petroleum Institute (API) that your Subcommittee should have a monthly accounting from the Coast Guard as to the possibilities of necessary insurance being reasonably available at realistic costs. We also believe that the Subcommittee should receive assurances by September from the Coast Guard backed by evidence or actual successful COFR applications that the shipping community is able to meet the strict requirements of the rule. Otherwise, the Coast Guard should modify or terminate its IFR.

Sincerely,

Ernest J. Corrado

Ernest J. Corrado
President

International Chamber of Shipping

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ICS/14/10

29 July 1994

Hon. William Tauzin
Chairman
Sub-Committee on Coast Guard and Navigation
U.S. House of Representatives
Room 1334, Longworth House Office Building
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BY TELEFAX: 010 1 202 225 0563

Dear Congressman,

HOUSE OF REPRESENTATIVES COAST GUARD SUB-COMMITTEE: HEARING ON THE INTERIM FINAL RULE ON CERTIFICATES OF FINANCIAL RESPONSIBILITY 21ST JULY 1994

Having attended the hearing of your Sub-Committee on 21st July, 1994 on the Interim Final Rule (IFR) relating to Certificates of Financial Responsibility (COFR) I thought it might be helpful for the record to summarise briefly the views of the International Chamber of Shipping (ICS) on the IFR.

As the principal international trade association for the shipping industry world-wide, ICS represents national associations of shipowners together comprising more than half the world's merchant tonnage (see membership list attached). In the context of the IFR it is therefore important to note that ICS reflects the interests of the owners and operators of all types of vessels, not only tankers.

Generally ICS shares the misgivings which you expressed about the IFR at the hearing. It is a matter of regret to ICS, as to other industry spokesmen, that the IFR has not attempted to solve any of the serious problems which the Notice of Proposed Rulemaking posed. In particular, the IFR does not make it possible for shipowners to use the overwhelmingly obvious, and hitherto unproblematic, method of providing evidence of financial responsibility: P&I Club cover.

We find it difficult to explain the Coast Guard's refusal to look for a solution which would enable the P&I Clubs to continue to act as oil pollution liability insurers in the United States. Perhaps the Coast Guard believed that once the IFR was issued shipowners trading to the United States would instruct their P&I Clubs to reverse their decision not to act as guarantors under OPA. If so, that was a dangerously false assumption, and owners stand squarely behind their Clubs in believing that the risks associated with acting as guarantors are too grave to be accepted.

The Coast Guard appears to be content to rely on the alternative methods of evidencing financial responsibility available under the IFR and the prospect of new insurance schemes

emerging to meet IFR requirements. There is little dispute that the only specific alternative methods, surety bonds and self-insurance, are relevant for only a small minority of owners: the American Petroleum Institute suggests one-third (a figure which ICS believes may be rather high) of the operators currently trading to the United States, leaving well over half to seek other alternatives.

So far only two new insurance schemes have emerged, Shoreline and Firstline. Both schemes remain shrouded in mystery and neither of them is apparently able to demonstrate firm reinsurance arrangements despite having had more than two years to prepare. ICS does not dismiss the possibility that such new schemes could develop, nor does it oppose the concept of alternatives to P&I Club cover for US oil pollution liability. It has, however, very grave misgivings about the ability of any such scheme, still in embryonic stage in late July 1994, to be sufficiently far advanced to offer a reliable service, fully established and approved by the Coast Guard, by the initial COFR deadline of 28 December 1994.

Quite apart from the question of whether shipowners will be able to obtain COFRs without relying on P&I Club cover, ICS questions how it can be in the interest of the United States to enact legislation and regulations which effectively exclude P&I Clubs from providing cover in US trades. P&I Club cover has provided a consistent, economical and highly effective system for compensation which has benefited shipowners and claimants alike. ICS is aware of no incidents in P&I history where the cover provided and the services rendered by P&I Clubs have failed the shipowner or the claimants in question. By issuing the IFR, the United States will in effect, have chosen to replace a reliable system with an impeccable record world-wide with an unknown and unproven system, and this without having achieved real benefits for claimants and possibly imposing unnecessary, extra costs on US consumers.

In sum, ICS finds it very difficult to believe that the United States would contemplate the possibility of a significant disruption of maritime transport to and from the United States as well as relying in future on shipping services which do not have the protection of the established P&I system.

We sincerely hope that the United States authorities will address the issues again and find practical solutions.

It must be recalled that Certificates of Financial Responsibility are only part of the problem. The broader problem posed by OPA is that of uninsurable, unlimited liability which the Mandatory Excess Insurance Facility proposal by Norway, Greece and Sweden has been created to address.

Yours sincerely

J.C.S. Horrocks
Secretary General

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1994 AUG -2 AM 8:41

July 27, 1994

Ms. Elizabeth Megginson
% Honorable William Tauzan, Congressman
2330 Rayburn Bldg.
Washington, DC 20515

Re: OPA '90
Certificates of
Financial Responsibility
Surety Bond Guarantees

Dear Ms. Megginson:

It has been suggested that I direct this letter to your attention in respect of the on-going discussions being held on Certificates of Financial Responsibility pursuant to the Oil Pollution Act of 1990.

I have been following with great interest the discussions being held amongst the USCG, Shipowners and Congress as to the availability of commercial solutions to the providing of COFRs as required by OPA '90. In light of these discussions, I would like to make an observation which no one has apparently seized upon as a vehicle to solving the impasse to the COFR problem.

When Congress passed OPA '90, it reaffirmed that there were four means of a Shipowner meeting the financial means test: 1) Certificate of Insurance, 2) a Surety Bond, 3) Self-Insurance Fund, & 4) Whatever else the USCG felt appropriate. It is evident that under #1 the P&I Clubs will no longer issue their Certificates, and that Shoreline and First Line are problematical and expensive alternatives. Numbers 3 & 4 have been ruled out for all practical purposes. Amazingly, however, there has been no discussion with anyone in the surety business about #2 which is the use of surety bonds as a serious vehicle for addressing the COFR problem; and I would submit that if this vehicle were better understood, both Congress and the USCG would find that a workable solution was readily available to meet both parties objectives. (After all, it was Congress in 1884 under the Hurd Act that mandated the birth of the surety industry to solve a very similar problem, and the surety industry continues today to serve as the vehicle to solve many Congressionally mandated requirements.)

I do not wish to bore you with how the technical aspects of bonding may apply to OPA '90, except to suggest that this very solution appears to have been passed over in deference to discourse over expensive and complex financing and reinsurance schemes which do not appear to be achieving the desired goals of providing a workable and financially secure vehicle which meets the intent of Congress.

If there should be any interest in your Committee as to how bonding might be used to address the problems Congress, Shipowners and the USCG are having, we would be more than happy to explain in greater detail.

Thank you for your time and interest.

Sincerely,
INTERNATIONAL SURETIES, LTD.

R. TUCKER FITZ-HUGH
President

Subcommittee on Coast Guard & Navigation
House Committee on Merchant Marine & Fisheries

FINANCIAL RESPONSIBILITY FOR WATER POLLUTION (VESSELS)

July 21, 1994

Comments by: George J. Ryan, President
Lake Carriers' Association

Lake Carriers' Association represents 98 percent of the tonnage carried in the domestic trade on the Great Lakes. Only a very small percentage of this cargo is liquid bulk products. The primary cargos carried are iron ore, coal, cement, sand, salt, potash, and grains. None of these cargos pose any environmental threat. Nevertheless, vessels owned by our member companies must comply with OPA 90 and with recently published U.S. Coast Guard regulations. Because the U.S. Coast Guard refuses to accept P&I Club membership as an asset, our members will incur an additional cost of $2,920,000 per year, if they are able to obtain Surety Bonds as evidence of the guarantee. This added cost will be borne by basic U.S. industries, primarily the steel industry which is in a life and death struggle with imported foreign steel.

As we have testified before, we believe that P&I Club membership can be treated as an asset just as several states presently consider P&I coverage as evidence of Financial Responsibility. Further, we believe that Congress does not preclude the U.S. Coast Guard from acting in a similar manner. It is well known that P&I Club membership generally provides $500,000,000 in coverage and in some cases up to $700,000,000. This coverage should be considered as a current asset in passing both the working capital and net worth financial tests. In fact, U.S. Government already defines current assets broadly. Federal EPA regulations for demonstrating financial responsibility for a hazardous waste facility, 40 CFR 264.141 (f) define "current assets" as follows: "cash or other assets or resources commonly identified as those which are reasonably expected to be realized in cash or sold or consumed during the normal operating cycle of the business." The phrase in bold, underlined print could reasonably include expected insurance proceeds for a particular occurrence.

U.S. Coast Guard refutes the above contention, and there is little we can do to convince them to the contrary. U.S. Coast Guard believes the U.S. shipowners control the P&I Clubs since they are members. However, U.S. shipowners do not represent a major interest in the clubs. Most members are engaged in trades other than to the United States and, thus, have no need to conform to rules that set a dangerous precedent. Thus, we ask this Committee to advise the U.S. Coast Guard that P&I Club Membership can be treated as an asset.

Our members make no threats about all commerce ceasing if P&I Club membership is not recognized as an asset. We do state categorically, however, that the added costs for surety bonds or for other commercial insurance, if they are available, will add significantly to the cost of doing business. For the stronger companies obtaining this insurance or bond it will be a financial burden to be passed on to the steel industry or the electric utilities; for the smaller companies, without the working capital requirements or net worth requirements required by a surety company or insurance company, there is a strong likelihood of being put out of business. While the larger companies may purchase these vessel assets, the added costs of raw materials could well make the difference between putting a U.S. company dependent upon low-cost materials out of business in favor of foreign suppliers.

If the cost of this insurance for surety bond led to a safer or environmentally better system of water transportation, the above costs might be bearable, but the expense will do nothing for safety or the environment. Congress can address this inequity by advising the U.S. Coast Guard that P&I Insurance is acceptable as evidence of financial responsibility.

GJR:cal
07/20/94

83-192 O - 94 - 9

Comments of

MARATHON OIL COMPANY

Regarding

U.S. Coast Guard's Interim Final Rule for
Vessel Certificates of Financial Responsibility

Submitted to

Subcommittee on Coast Guard and Navigation
Committee on Merchant Marine and Fisheries
U.S. House of Representatives

August 23, 1994

Marathon Oil Company is an integrated petroleum company involved in worldwide exploration, production, transportation and marketing of crude oil and natural gas; and domestic refining, transportation and marketing of petroleum products. Marathon ranks as the nation's eighth largest refiner, and annually supplies some 10 billion gallons of refined petroleum products to U.S. markets.

Marathon Oil Company appreciates the opportunity to inform the Subcommittee of its views of the U.S. Coast Guard's (USCG) interim final rule on vessel certificates of financial responsibility (COFR). The Subcommittee is to be commended for holding hearings to determine the impact of these critical regulations. In Marathon's view, the COFR rules have the potential to significantly impair the financial well-being of a large segment of the petroleum industry, to disrupt supplies of crude oil and petroleum products imported to the United States, and to increase U.S. energy costs, which will harm the nation's competitive position in world markets and unnecessarily increase prices for American consumers.

Intra-industry competitive impact

The COFR regulations will place Marathon at a competitive disadvantage relative to larger competitors who operate their own fleets.

Marathon Oil Company does not own or operate any crude oil tankers. Consequently, Marathon relies heavily on independent tanker vessels to transport the imported crude oil necessary to supply our four domestic refineries. The COFR regulations will require independent tanker owners to buy some form of COFR financial security, since most independents do not have sufficient financial resources to self-insure. The costs to purchase COFR financial security will have to be passed along by independent vessel operators to cargo owners in the form of higher rates, which will increase significantly our raw materials costs.

Marathon's larger competitors who own their own fleets have much less need for independent tankers. Further, the USCG regulations require that fleet owners only have to self-insure a guarantee for *the single largest tanker in their fleets*, which provides a significant competitive advantage over companies who must rely on independent tankers. Marathon believes strongly that the USCG has interpreted too narrowly the OPA 90 law in this respect and, as a result, has unfairly penalized a large segment of the petroleum industry (i.e., those companies that rely heavily on independent tankers to transport their crude oil requirements).

Although permitted to do so under the COFR regulations, as a practical matter Marathon Oil Company cannot provide the necessary financial guarantees on behalf of the ship owners who transport our crude. Marathon currently imports about 100 million barrels of crude oil per year, via about 95 separate shipments -- approximately eight shipments a month. Based on our interpretation of the regulations, to meet the COFR requirements on behalf of the ship owners, it would be necessary for Marathon to have in place financial guarantees sufficient to cover approximately two months' shipments. This would require financial resources of sufficient magnitude to guarantee a cumulative total of roughly <u>$1.9 billion</u> outstanding at any one time! Simply stated, this represents an impossible burden for Marathon.

To further the analysis, Marathon has calculated that use of surety bonds would increase our crude oil transportation costs by $21 million per year. Alternatively, use of the new Shoreline facility would add $11 million in delivered crude costs. These represent significant costs that our larger

competitors with their own fleets would not face since, presumably, each would self-insure only its single largest vessel. To the extent these competitors supplement their own fleets with chartered vessels, they could have similar problems -- but with a much smaller impact since they have their own fleet vessels to deliver most of their crude oil needs.

Wasteful new insurance regimes

In Marathon's view, it is wasteful to add new forms of costly financial security into the COFR procedures when essentially all tankers already have good P&I insurance. P&I insurance has a proven record of paying for pollution cleanup expenses. Furthermore, the P&I insurers have never stated they will not insure OPA 90 liabilities; they have said they will not provide claimants other than their ship members with guaranteed protection. Although P&I administrators have problems with the OPA 90 law and with the interim regulations, we are unaware of any constructive meeting where the principals of the P&I associations and of the Federal entities have met to sort out suggested changes that would result in an acceptable compromise. It is critical that such a meeting take place.

It should be noted that new commercial market alternatives (to P&I insurance) have been explored, but they all appear to have inordinately high costs. And these new costs would be in addition to the existing costs of P&I insurance. For example, the costs of Shoreline Mutual and surety bonds are estimated to be $.116/barrel and $.22/barrel, respectively. These costs contrast sharply with those of the Oil Spill Liability Trust Fund, which charges $.05/barrel, or with $.01/barrel for

the current P&I surcharge at LOOP. Given the competitiveness of world markets, the United States cannot afford to unnecessarily inflate its crude oil costs. By necessity, these cost increases will be translated into higher commercial and consumer prices. The result: manufactured goods that cannot compete in world markets, and artificially inflated costs for American consumers.

Internalized costs prompt vessel owners to operate safely

The incidence of cost of OPA 90 compliance must originate in the tanker/transportation segment of the petroleum business to properly assure that ships bear responsibility for their actions. It is logical to assume that if the initial payment response to a spill is borne by the vessel, and if future insurance premiums reflect past loss history, the vessel operator will exercise more diligence in conducting safe operations. Therefore, any reliance on the other non-remunerated guarantors is counter-productive to the goal of OPA 90 -- i.e., to encourage safe tanker operations. THE USCG itself has argued in its Regulatory Impact Analysis that the costs of compliance should be "internalized" in the operation of the vessels (p. 39).

Independent expert opinions needed

Congress and regulators should seek out expert opinion from insurance brokers as to the applicability of commercial COFR options to most vessel compliance -- not just the few strong fleets. Upon close examination, it can be determined that the majority of oil imports that arrive aboard

independent oil tankers do not qualify for surety bonds or self-insurance. Furthermore, the proposed facilities such as Shoreline Mutual are still undercapitalized and are hoping for a strict COFR regime to provide them with a monopolistic opportunity. All the major international insurance brokers and many regional insurance brokers employ experts in marine operators and insurance. Our own inquiries with these experts have not uncovered any commercial solutions to the COFR requirements for the majority of ship owners. We challenge others to make similar inquiries.

Supply disruptions

In the debate over the USCG's COFR regulations it has been suggested that, if indeed there are problems in meeting the financial responsibility requirements, only a subset of the shipping industry will experience difficulties. By inference, any resulting supply disruptions will be "minor" in scope and, therefore, should not cause concern. But past history has clearly demonstrated that even the threat of "minor" oil-supply disruptions can result in dramatic price responses for crude oil and refined petroleum products. Any disruption of petroleum supplies will likely result in significant price volatility and higher consumer prices for gasoline, diesel fuel and heating oil (as petroleum marketers attempt to secure supplies of these products to meet their customers' needs). Simply stated, it is poor public policy to implement regulations that "experiment" with unproven financial-security regimes, given the significant economic disruption that could result.

* * *

SEP 06 1994

1994 AUG 32 AM 11: 07

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August 23, 1994

C. JAMES PATTI
President

The Honorable Billy Tauzin, Chairman
Subcommittee on Coast Guard and Navigation
541 Ford House Office Building
Washington, DC 20515

Dear Mr. Chairman:

On behalf of American Heavy Lift Shipping Company I am pleased to submit the attached statement for the record in conjunction with your Subcommittee's hearing on the Coast Guard's Interim Final Rule on financial responsiblity as required by the 1990 Oil Pollution Act. The Maritime Institute fully endorses the views expressed by American Heavy Lift, and we wish to associate ourselves with AHL's remarks.

As demonstrated during your July 21 hearing, there are serious albeit unintended consequences resulting from the implementation of OPA-90 which may further weaken the United States-flag merchant marine without contributing to the protection of the marine environment. Clearly, a company like American Heavy Lift, which is committed to using its resources to construct double hull cargo carrying forebodies for its vessels in order to build upon its exemplary safety record should not be forced to divert these resources to areas which do nothing to prevent oil spills. Dedicating resources to improved crew training techniques and more modern equipment helps protect the marine environment whereas the expenditure of more and more resources for insurance only enriches insurance underwriters.

On behalf of the Maritime Institute and American Heavy Lift, I wish to thank you for your efforts in support of the United States-flag merchant marine. We stand ready to work with you and your staff to ensure that the implementation of OPA-90 achieves its objectives in a manner which allows for the operation of modern, safe United States-flag ships.

Sincerely,

C. James Patti
President

SEP 06 1994

AHL

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August 22, 1994

Congressman W. J. Tauzin
Subcommittee on Coast Guard and Navigation
Room 541, Ford House Office Building
Washington, D.C. 20515

Dear Mr. Chairman:

American Heavy Lift Shipping Company (AHL) owns and operates four 34,000 DWT United States-flag coastwise eligible petroleum product tankers. AHL, headquartered in New Orleans, annually employs 300 seagoing personnel and nine office staff. Our realistic overhead structure and seagoing wage rates are among the domestic maritime industry's most cost effective, as AHL strives to become more nationally and internationally competitive and even more operationally safe and sound.

We greatly appreciate your efforts in regards to the Coast Guard's Interim Final Rule on financial responsibility required by OPA-90. As an owner and operator of tankers, AHL will be required to submit by December 28, 1994, evidence of financial responsibility that meets the Coast Guard's requirements. These requirements can and will seriously impact American Heavy Lift and impose a financial burden totally out of proportion with the intended goals and objectives of the statute.

All of AHL's vessels are employed in the U.S. coastwise trade and annually deliver about 1.2 billion gallons of gasoline, home heating fuels and jet fuels for consumption by U.S. end users.

Safe, effective, mistake free operations have become AHL's goal since inception and the company's lifetime spill ratio of .00000001% although excellent, does not meet AHL's stated goal of zero oil discharged. To that end the AHL management team and seagoing employees have long since dedicated themselves to meet head on the rigorous, but necessary tests of OPA-90.

Accordingly, AHL has spent considerable dollars and countless hours upgrading every aspect of our operational abilities while constantly checking and rechecking our logic, attitude, form and substance regarding the importance, the dangers and intense responsibilities of transporting petroleum products. Without question this has been time and money well spent.

The AHL team looks with pride upon our frequent oil spill practice drills and intense training programs and how these serve to heighten awareness and create precision operational

methods and response actions. Vessel crews and terminal personnel now work in friendly professional concert with respect to mistake free cargo transfer technique and environmental protection.

AHL for the past 16 months has been working closely with Avondale Industries to design and build OPA-90 double hull cargo carrying forebodies that will meet all national and international requirements and the environmental challenges of the future. These four vessels will require more than two years construction time and will steadily employ approximately 500 Avondale Shipyard workers and will provide AHL employees and customers with environmentally safe tonnage designed for effective product transportation.

Through the years AHL has relied upon membership in the Standard Steamship Owners P&I Association to provide needed marine insurance cover and has used this cover, through a letter of undertaking issued by the club, satisfied COFR requirements under prior law. Via the Standard Club, AHL currently has pollution coverage in the amount of $700 million.

In that the clubs are unwilling to become COFR guarantors, AHL is therefore exploring alternative methods of satisfying the COFR requirements. AHL wishes to adamantly correct the misperception that club members have the ability to direct the clubs to submit to U.S. COFR requirements. As a small owner/operator, AHL's business represents only a fraction of the club's membership. AHL does not sit on the board of the club and has no influence on club policies and decisions. The club's cartel like structure precludes withdrawal from individual clubs without sizeable penalty and greatly inhibits competition. This structure has enabled their industry to raise annual premiums substantially over the past several years. AHL's P&I premiums have risen from about $350,000 per annum with a $10,000 per event deductible to our current $1.2 million annual premium with a $50,000 per event deductible. As far as AHL can determine these increases have not resulted in real additional coverage for AHL nor have the clubs assumed greater risks.

As a result of OPA's direct action requirement and other restrictions upon guarantors providing evidence of financial responsibility, the Standard Club will not provide a COFR guaranty and AHL is placed in the undesirable situation of having to seek the required guaranty from an alternative source. The only option available to AHL is to obtain additional insurance. Because of it's size and financial structure, AHL will not be able to self-insure under the IFR. Similarly, AHL does not believe that it will be able to find a guarantor willing to provide a CFR guaranty. When taking into account the "net quick" cash requirements, a surety bond becomes an option of no viability.

Accordingly, AHL may be forced to turn to the new entities being formed specifically to provide COFR coverage. In addition to being extremely costly, (current estimates for AHL are about $350,000 per year plus insurance calls of a like amount) participation in a scheme such as that being developed by Shoreline Mutual will violate the double insurance rules of the P&I clubs. (Current Club correspondence have stated such). As a result, AHL's pollution cover of $700 million may no longer be available. AHL would then be forced to operate with less pollution cover, thereby exposing the company to uninsured risk.

Whereas the company now operates with $700 million of cover through the Standard Steamship Association, under the IFR it will only be required to provide evidence of financial responsibility in the amount of $30,207,000 which is the limitation amount for AHL's largest vessel.

The net "plain talk" is that AHL will be forced to spend more money for less pollution coverage and will have less dollars to spend effectively and logically on better operational techniques and on modern double hull tonnage. Dollars and time spent on better operational techniques via training and double hull petroleum cargo carrying space via capital expenditures will help prevent spills: more dollars for less effective spill insurance coverage will not prevent oil spills. The COFR interim final rule enriches the insurance underwriters. Better training and modern equipment enriches the U.S.'s precious environment.

Consequently, we ask your help to delay the implementation of the Coast Guard's Interim Final Rule until such time as its requirements can be restructured in order to truly protect the marine environment without unnecessarily affecting safe, efficient and environmentally-conscious vessel operators which, like American Heavy Lift, have adequate marine insurance coverage through membership in a P&I Association.

Sincerely,

Richard D. Horner
President

WILMER, CUTLER & PICKERING
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November 7, 1994

The Honorable W. L. Tauzin
Chairman, Subcommittee on Coast Guard
and Navigation
Committee on Merchant Marine and
Fisheries
U.S. House of Representatives
Washington, D.C. 20515-6230

Re: Shoreline Mutual Insurance

Dear Mr. Chairman:

On behalf of Shoreline Mutual Insurance, I am writing to respond to the questions enclosed with your letter of September 2, 1994. I apologize for the delay in this response; as you know, we did not receive your letter until September 30, 1994.

The questions, and Shoreline's answers, are as follows:

Question No. 1: During the hearing, I requested a list of the organizations that Shoreline sent to solicit re-insurance and what reinsurance has Shoreline secured since the hearing?

Answer No. 1: Shoreline has a completed reinsurance contract placed by Willis Faber North America in New York. The reinsurance program has already been approved by the United States Coast Guard (see attached letter from Mr. Daniel F. Sheehan dated October 19, 1994), which has described it in the press as a "beautiful reinsurance package," and by the Bermuda regulatory authorities. The reinsurance program is to cover $290 million excess of $10 million, any one accident, per ship entered, and in the aggregate in one year, with a facility for two free reinstatements. The identities of the companies participating in the reinsurance package are, however, confidential.

Question No. 2: What type of reinstatement policy will Shoreline have for its members if they have a spill and file a claim? What will be the reinstatement policy with the reinsurers?

Answer No. 2: Shoreline provides coverage to members for an unlimited number of oil spill liabilities within the policy year. Shoreline provides this coverage by using the traditional mutual P&I system, according to which members pay for claims, reinsurance and administration by means of advanced and supplementary calls. Shoreline has designed tariffs so that advance calls will, in all normal circumstances, be sufficient to meet all the anticipated expenditures, and so that supplementary calls will only be necessary where the aggregate total of claims in one year exceeds the amount of Shoreline's standing funds for claims contingencies ($300 million), and the aggregate of its reinsurance coverage available in one year ($870 million).

Question No. 3: Does Shoreline believe that they are completely protected in U.S. courts against direct action and unpaid claims from a spill where the owner is unable to pay because Shoreline will be the guarantor?

Answer No. 3: Shoreline's position in respect of this point was expressed in detail in Hugh Bryant's testimony to the Coast Guard and Navigation Subcommittee on July 21, 1994. Shoreline accepts the Coast Guard's wording in the Interim Final Rule and in the text of the COFR guarantee, and the express wording of section 1016(g) of OPA as being sufficient to ensure that any direct action against Shoreline is limited to the face value of the guarantee.

Question No. 4: Does Shoreline believe they can be approved and operational in time to provide adequate opportunity for negotiating contracts with vessels owners for a COFR, especially for vessels calling to the U.S. within the first few months after the December 28th compliance date?

Answer No. 4: Shoreline is fully confident that it will be approved and operational in good time.

Question No. 5: If Shoreline is not approved by the Coast Guard in time to commence operations and provide evidence of financial responsibility for vessel owners, would you request the Coast Guard to suspend the compliance date?

Answer No. 5: Shoreline is confident that this hypothesis will not arise, on the grounds that it will be fully operational and approved in good time.

Question No. 6: Could you provide a comparison between what it would cost vessel owners for a few different size vessels for a COFR under Shoreline's coverage and what is required now (pre-OPA)?

Answer No. 6: Shoreline is not privy to details of premiums paid by individual ship owners to the P&I clubs. Shoreline is only in a position to give information relating to its own pricing, which has already been passed on to the Subcommittee. However, that pricing must now be looked at in the light of a recent development relating to Shoreline. Shoreline will now operate as an excess insurance to top up the cover provided by the P&I clubs in the International Group. Shoreline's amended tariffs are copied herewith.

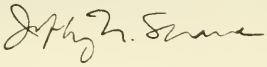
With reference to Congressman Lancaster's question -- whether the new COFR regulation will result in shipowners getting reduced insurance at much higher cost -- the realignment of Shoreline as an excess insurer on top of the P&I club coverage means that in fact the aggregate cover available to shipowners has been increased by Shoreline from $500 million or $700 million to either $800 million or $1 billion, depending on whether the shipowner avails itself of the $200 million excess insurance facility as well. In other words, there will be a net increase in coverage, not a loss, as a result of Shoreline's insurance. The P&I clubs, with whom representatives of Shoreline have met recently, have indicated that they now consider that there is no double insurance involved in Shoreline, when compared with their own coverage.

I hope the comments above respond fully to your questions and that of Congressman Lancaster. At the same time, I enclose for your attention a copy of a statement

released on October 27, 1994, at an open meeting for the public, arranged to explain to interested parties the latest developments relating to Shoreline. I think you will find this statement very useful in dealing with any other questions you might have.

If I can furnish any further information, please do not hesitate to let me know.

Sincerely,



Jeffrey N. Shane
Counsel to Shoreline Mutual
Insurance

Enclosure

cc: The Honorable H. Martin Lancaster

Greek Shipping Co-operation Committee

6, Middlesex Street, London E1 7EP - Tel. (+44 71) 247 3773 - Fax (+44 71) 375 2046 -Telex 886255 GRSHIP G.

The Honourable Billy Tauzin,
Chairman, Subcommittee on Coast Guard and Navigation,
Committee on Merchant Marine and Fisheries,
United States House of Representatives,
Room 1334, Longworth House Office Building,
Washington, D.C. 20515-6230,
U.S.A.

29 July 1994

Dear Mr. Chairman,

HEARING ON INTERIM FINAL RULE FOR VESSEL CERTIFICATES OF FINANCIAL RESPONSIBILITY

On behalf of the Union of Greek Shipowners, Norwegian Shipowners' Association, Swedish Shipowners' Association, and the Greek Shipping Co-operation Committee, we should like to congratulate you and the members of your subcommittee for your timely initiative in calling the July 21 hearing. Your understanding and appreciation of the difficulties being faced by the U.S. and international shipping industry in complying with the Interim Final Rule for vessel financial responsibility under the Oil Pollution Act of 1990 was a source of great encouragement.

We should also like to thank you for the invitation to our organisations to testify on the related subject of the Mandatory Excess Insurance Facility (MEIF). As you are aware, Mr. Chairman, we consider the combination of resources currently available to provide funds for compensation for oil pollution damages, consisting of Protection and Indemnity Association and insurance market indemnity insurance, the assets of the shipowners and the U.S. Oil Spill Liability Trust Fund, to be inadequate in light of recent experience. The MEIF would strengthen the regime substantially, to the benefit of the international shipping industry and U.S. public alike.

At the July 21 hearing you questioned why the MEIF was needed if OPA already has an "insurance fund", namely the Oil Spill Liability Trust Fund. The Trust Fund, in structure and in practice, does not function as an insurance fund. It pays claims to third parties but not for the benefit of shipowners as an insurance fund would. When the Trust Fund pays claims the shipowner must assume that the Trust Fund will seek to recover these amounts from the shipowner under rights of subrogation. For claims in excess of OPA limits, the Trust Fund is expected to break the shipowner's limit of liability and exhaust the owner's insurance and assets, if necessary, in pursuit of full recovery. Moreover, the Trust Fund does not protect shipowners from state liability

laws, which generally do not have limits. The MEIF would address this massive liability exposure by adding $1.5 billion of insurance to the shipowner's standard P&I coverage.

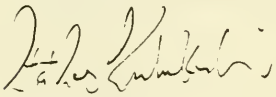
Mr. Chairman, the MEIF as proposed would not be an extension of Big Government. Its funding is to be private, not from government coffers. No taxation is involved. The MEIF is budget-neutral. In no way does the MEIF duplicate the Oil Spill Liability Trust Fund; to the contrary, the privately-funded MEIF complements and protects the tax-funded Trust Fund, thereby also providing a measure of protection to the Coast Guard budget.

In order to preclude the possibility of underinsured vessels gaining a competitive advantage, it is essential that such an excess insurance facility be mandatory upon all vessels engaged in the international ocean going petroleum trades, and it is, thus, necessary to turn to Congress for legislative assistance. Our proposal calls for a facility organised pursuant to an Act of Congress as a not-for-profit, tax exempt, "government sponsored enterprise" (but not a government enterprise). I must emphasise, it would be financed entirely from the private sector. Moreover, it would be managed independently of the U.S. Government and would, in the long run, be entirely self sustaining.

The modest involvement of the U.S. Congress in establishing such a facility would strengthen very substantially the resources available for oil pollution compensation, providing an effective, fair and durable solution to the twin problems of vessel financial responsibility guaranties under OPA 90 and adequacy of sources of funding for oil pollution compensation, to the great benefit of all concerned.

I ask that this letter be made a part of the record of the hearing. Thank you very much for your consideration.

Very truly yours,



Stathes Kulukundis,
Deputy Chairman,
Greek Shipping Co-operation Committee

U.S. Department of Transportation
United States Coast Guard

Director
United States Coast Guard
National Pollution Funds Center

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Arlington, VA 22203
Staff Symbol: cm
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5730
OCT 6 1994

The Honorable W.J. (Billy) Tauzin
Chairman, Subcommittee on Coast Guard
and Navigation
Committee on Merchant Marine and Fisheries
U.S. House of Representatives
Washington, DC 20515-2201

Dear Mr. Chairman:

At the COFR Hearing on July 21, 1994, you indicated that you thought the Oil Spill Liability Trust Fund (OSLTF) was experiencing only limited use. I thought you might be interested in the enclosed statistics which indicate use of the Fund within the Eighth Coast Guard District.

If I can provide further information on the Fund, please let me know.

Sincerely,

Daniel F. Sheehan

DANIEL F. SHEEHAN
Director, National Pollution Funds Center

Encl: (1) Eighth CG District Totals

Eighth Coast Guard District by Fiscal Year Totals As of 30 September 1994

FY	# Cases	Ceiling	Expenditures	Billed	Recovered
1990	12	$1,389,049.20	$1,389,049.20	$1,381,158.09	$ 28,232.56
1991	70	$1,310,606.00	$1,310,606.00	$1,273,728.82	$1,006,736.21
1992	115	$2,219,536.00	$2,219,536.00	$2,218,979.84	$1,031,878.29
1993	117	$3,035,519.00	$1,480,899.35	$ 795,936.94	$ 512,892.18
1994	114	$4,471,257.00	$ 584,576.90	$ 97,193.39	$ 72,954.97
Totals	**428**	**$12,425,967.20**	**$6,984,667.45**	**$5,766,977.08**	**$2,652,694.21**

Explanation of Terms:

Ceiling - amount allocated to Federal On-Scene Coordinators for removal actions for oil spills.
Expenditures - actual costs incurred. Some responses still are in progress or NPFC is awaiting documentation so costs are less than the ceiling amounts.
Billed - these are costs incurred and billed to responsible parties. Circumstances preclude identification of responsible parties in every case, so total billed amounts are always less than total expenditures.
Recovered - the amounts actually collected from responsible parties to date.

ONE HUNDRED THIRD CONGRESS

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U.S. House of Representatives
Committee on
Merchant Marine and Fisheries
Room 1334, Longworth House Office Building
Washington, DC 20515-6230

November 2, 1994

President William J. Clinton
The White House
1600 Pennsylvania Avenue, NW
Washington, D.C. 20500

Dear Mr. President:

We are writing to express our concerns about the effects of the initial implementation date for the Final Rule issued by the Coast Guard on July 1, 1994, requiring Certificates of Financial Responsibility for vessels. The Final Rule implements the requirement, under section 1016 of the Oil Pollution Act of 1990 (33 U.S.C. 2716)(OPA '90), for owners or operators of vessels to obtain evidence of insurance or other evidence of financial responsibility to cover their potential oil spill liability under OPA '90. The Final Rule requires U.S. and foreign oil tankers in U.S. waters to be covered by Certificates of Financial Responsibility issued by the Coast Guard by an "initial implementation date" of December 28, 1994.

We believe that the December 28, 1994, deadline for compliance with the Final Rule may cause a serious disruption of our nation's imported oil supply. The deadline may not allow enough time to conclude charter arrangements for oil shipments and complete voyages of oil tankers from the Persian Gulf to the United States. We understand that it takes approximately 37 days for a vessel to arrive in the Gulf of Mexico from the Persian Gulf. It also takes approximately 2 weeks to complete charter arrangements for an oil shipment. This does not include the additional days needed for lightering and transshipment of oil to U.S. ports. No one can state with certainty when all U.S. and foreign oil tankers must be covered by Certificates of Financial Responsibility to avoid a disruption of our imported oil supply. Obviously, however, we are nearing the date when a disruption of our oil supply is inevitable if Certificates of Financial Responsibility are not available.

THIS STATIONERY PRINTED ON PAPER MADE OF RECYCLED FIBERS

The effects of a disruption in our foreign oil supply would be disastrous. Close to 75 percent of the crude oil and approximately two thirds of the refined product imported into the United States in recent years was carried aboard independent vessels. If independent vessel owners cannot obtain Certificates of Financial Responsibility from the Coast Guard because of unavailability of affordable insurance, there will be a major shortfall in our oil supply. If the supply of oil to the independent refineries is disrupted, shortages will occur not only in gasoline and heating oil, but also in jet fuels, fuels for military aircraft, and electricity production. The gasoline lines in this country following the 1973-1974 Arab oil embargo were caused by a shortfall of less than 6 percent of the nation's domestic consumption. Obviously, there is a potential for a much greater disruption under the present circumstances.

Another concern of ours involves the Coast Guard's position that it is appropriate for cargo owners to obtain surety bonds or otherwise enable a tanker owner to obtain a Certificate of Financial Responsibility on a voyage-by-voyage basis. Several of us were members of the Conference Committee for the Oil Pollution Act of 1990 that specifically rejected cargo owner liability for oil spills. The responsibility for insurance coverage lies with the vessel owner, and it is not acceptable to require cargo owners to indirectly assume a vessel owner's liability because no suitable insurance alternative exists.

This year, about 45 percent of our foreign oil supply has been imported by independent oil refineries. Independent oil companies simply cannot afford to act as cargo guarantors. A disruption of oil supply to independent refineries would have disastrous effects on their businesses and employees, as well as on the businesses and consumers who depend on them to supply their products.

Finally, we are concerned because there may be many safe, responsible vessel owners who are unable to obtain Certificates of Financial Responsibility using the insurance options currently available. The regulations implementing the requirement for Certificates of Financial Responsibility should not cause U.S. or foreign vessel owners who operate safely in U.S. waters to go out of business. This would concentrate control of oil transportation resources, and have an anticompetitive impact in the world oil market. If safety is not an issue, market forces should control who operates in the international oil transportation business. Implementation of the certificates of financial responsibility requirement under OPA' 90 should not control the supply of vessels that are available to transport oil to the United States.

We encourage you to delay implementation of this Final Rule until there are insurance options available, which are both affordable and reliable for U.S. and foreign vessel owners to obtain Certificates of Financial Responsibility from the Coast Guard. The consequences to our economy and to the citizens of our country of forcing a premature deadline are simply too great to risk.

Sincerely,

W. J. (Billy) Tauzin
Chairman
Subcommittee on Coast Guard
and Navigation

Jack Fields
Ranking Republican Member
Committee on Merchant Marine
and Fisheries

Solomon P. Ortiz
Chairman
Subcommittee on Oceanography,
Gulf of Mexico, and the
Outer Continental Shelf

Howard Coble
Ranking Republican Member
Subcommittee on Coast Guard
and Navigation

Greg Laughlin
Member of Congress

Herbert H. Bateman
Ranking Republican Member
Subcommittee on Merchant
Marine

cc: The Honorable Federico Pena
The Honorable Lloyd Bentsen
The Honorable Hazel R. O'Leary
The Honorable Alice M. Rivlin
The Honorable Thomas F. "Mack" McLarty III

CERTIFICATES OF FINANCIAL RESPONSIBILITY
A COST BENEFIT DISCUSSION

The present Certificate of Financial Responsibility rulemaking presents an excellent opportunity to examine regulatory costs in terms of the value received.

Background

OPA-90 created a scheme to finance oil spill damages and clean-up costs that involves contributions by both the spiller and the owners of the oil. In the marine transportation context, the shipowner is liable for these costs up to a limit of liability. Above that, the risk is spread to cargo owners and their customers through a tax on refinery receipts. This tax finances the $1 billion Oil Spill Liability Trust Fund. If the shipowner fails to respond to a spill, this fund will also pay the shipowner's share of the cost so that all injured parties are assured of compensation and funds are always available to clean up the spill.

A shipowner's limit of liability is based on vessel size. The average large tanker that enters U.S. ports would have a liability limit of approximately $115 million.[1] Shipowners mutualize oil spill liability with other shipowners through Protection and Indemnity Clubs which insure 95 percent of the oceangoing fleet. Standard P&I coverage for oil spills is $500 million, about $475 million of which is underwritten by Lloyds of London through a reinsurance contract with the P&I clubs. The clubs are organized to reimburse or "indemnify" shipowners for the costs incurred in paying covered liabilities.[2]

Under this mutualization and reinsurance scheme, the major portion of oil spill liability risk is spread internationally through premiums or "calls" on all club members. Another portion is concentrated in the United States through a "per-call" surcharge on shipowners whose tankers call here. To manage these risks, the Club rules require the shipowners to mitigate damages[3] and operate their ships in a responsible manner.

To maximize the probability that a shipowner's funds will be available to respond to an oil spill, OPA-90 calls upon the Coast Guard to issue Certificates of Financial Responsibility based upon a showing that the shipowner is financially capable of responding to a spill up to the limits of liability. OPA-90 also states that anyone who provides evidence of financial responsibility for the shipowner will be considered a "guarantor" and be subject to direct suit by injured parties.

The P&I clubs have indicated that they would not be interested in insuring the additional risks associated with becoming guarantors under OPA-90 and would not be in a position

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[1] This assumes a 150,000 deadweight ton tanker which is about the size of the average large tanker that enters U.S. ports The $115 million includes $5 million which is the maximum limit of liability under CERCLA

[2] This is generally called the "pay-to-be-paid" rule.

[3] Called the "sue-and-labor" rule.

to provide evidence of financial responsibility under a regulatory system which furthered this concept. Although Lloyds has not spoken as an institution on the issue, the indications are that those underwriters would not be interested in this business either.[4] Thus, under any rule that contains guarantor status for insurance companies, P&I insurance generally would not be available to shipowners to provide evidence of financial responsibility.

Seventy percent of the crude and petroleum products transported by water in the United States are carried by relatively small independent shipping companies.[5] A similar, if not greater, percentage of small operators carry the imported oil that makes up about 50 percent of America's petroleum consumption. Without the ability to use P&I insurance to demonstrate the ability to respond to an oil spill, most of these small shipping companies could not qualify for a COFR.[6]

Despite this reality -- and a great deal of discretion in the matter -- the Coast Guard appears intent on issuing a final rule that would require these independent shipowners to provide guarantors for their liabilities thus eliminating P&I insurance as an option for establishing financial responsibility. While acknowledging this could cause economic chaos, the agency appears to justify this regulatory approach with the assumption that their proposed rule will create a new insurance market and a new insurance facility will emerge to provide guaranties for these smaller companies. In fact, promoters of two new Bermuda-based companies have provided comments to the rulemaking docket indicating that they would insure shipowners and guarantee their liability for oil spills under federal law. One such group has also publicly stated that they would require $400 million in premiums to issue the guarantees needed under the Coast Guard's proposed rule. These premiums would be in addition to existing P&I "calls" as it is believed that no shipowner would be willing to give up its existing insurance.

This is the best case.[7] Many commentators have observed that the likelihood of this new facility emerging is small particularly due to the reluctance of Lloyds to reinsure these risks. Nevertheless, it provides a basis for comparing costs versus benefits of the proposed rule.

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[4] See quote of Richard Youell, a leading Lloyd's underwriter in Lloyd's List, April 23, 1994: "You can lead a horse to water but you cannot force an underwriter to drink the poisoned draughts of the Oil Pollution Act."

[5] Final Report, Economic Analysis of Alternatives for demonstrating Financial Responsibility under the Oil Pollution Act of 1990, Nathan Associates Inc, April 14,1994.

[6] Ibid

[7] Most commentators predict a rationalization of the fleet serving the country providing a shortage of vessels to carry its commerce as the most probable consequence of the proposed rule.

Benefits

Oil spills of any consequence aren't regularly happening in the United States as the Coast Guard and cargo owners have been doing an excellent job of screening vessels that come here. Thus, the risk of an oil spill occurring that would test the performance of the P&I system is small. Moreover, the P&I clubs' performance in supporting their members in the United States and worldwide has been outstanding. Consequently, the risk of a shipowner defaulting on its obligations because a P&I club didn't perform are small as well. Combining these probabilities, the risk of the Oil Pollution Fund having to pay the shipowner's share of a spill is even smaller yet.[8] Nevertheless, it could happen, and for the sake of debate we could assume a very conservative five percent annualized occurrence rate.

A convenient method of monetizing the cost of such occurrences for analytical purposes is to multiply the probability of something happening times the cost of that occurrence. In this case, it would be 5% times the high average limit of liability of $115 million. The product is $5.75 million a year. This represents the potential annualized cost to the fund and, conversely, the presumed value of a regulatory regime designed to create a market for a new insurance facility that would provide guaranties for shipowners.[9]

Cost

Assuming that a new facility will emerge to guarantee the shipowner's performance, the cost to the American economy of creating these guarantors for the shipowners will be about $400 million.[10]

Conclusion

Considering only one year's premium, the cost of this regulation exceeds the benefit by almost 70 times. Moreover, the same consumer base will pay the $400 million cost of guarantors as would be paying the $5.75 million potential cost to the fund if no guarantors were in place. The President has ordered that: "Each agency shall assess both the costs and the benefits of the intended regulation and, recognizing that some costs and benefits are difficult to quantify, propose or adopt a regulation only upon a reasoned

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[8] Commentators on the rulemaking have proposed alternative approached that would reduce this risk even further while allowing the use of P&I insurance. See December 17, 1993 comments to the regulatory docket by "A Coalition of Eight American Shipping Companies."

[9] Guarantor status also contemplates direct suits by injured parties against the guarantor. The reader is left to evaluate the positive or negative aspects of this attribute, particularly in face of the administrative alternative provided in OPA-90 for the administrative settlement of claims by the Oil Spill Pollution Fund.

[10] Some of this premium will return to the United States in the form of claims payments. However, the existing P&I system will return the same amount so this $400 million is considered the costs of the "guaranty" that will protect against the need for the fund to pay out $5.75 million annually due to P&I insurance failure

determination that the benefits of the intended regulation justify its costs."[11] Regulatory alternatives have been suggested that are within the Coast Guard's discretion and which would allow the use of P&I insurance with little or no additional cost to the economy. These alternatives should be presented to the public in regulatory language so that they can be thoroughly evaluated.

06/11/94

[11] Executive Order 12886, September 30, 1993

SEP 06 1994

United States Department of the Interior

MINERALS MANAGEMENT SERVICE
Washington, DC 20240

AUG 31 1994

Honorable Gene Taylor
House of Representatives
Washington, D.C. 20515

Dear Mr. Taylor:

I was recently informed that at the July 21, 1994, hearing before the Merchant Marine and Fisheries Subcommittee on Coast Guard and Navigation on vessel Certificates of Financial Responsibility (COFR) you inquired on the status of rulemaking with regard to COFR requirements for "offshore" facilities, including small fuel operations. I am pleased to be able to provide you with the following information.

The Minerals Management Service (MMS) is taking a cautious and deliberate approach to implementing the requirements of section 1016(c) of the Oil Pollution Act of 1990 (OPA 90). On August 25, 1993, we published an Advance Notice of Proposed Rulemaking (ANPR) focused on OPA 90 oil spill financial responsibility requirements for "offshore" facilities. Within the ANPR, we indicated the kinds of "offshore" facilities within the navigable waters of the United States that may be subject to the oil spill financial responsibility requirements of OPA 90, as derived from the language and legislative history of section 1016. This ANPR was published to help us gather information used to identify and document the effects of these requirements and to identify alternative approaches to structuring a future Proposed Rule.

We published this ANPR to ensure that those who may be affected by a future Proposed Rule would have the fullest opportunity to participate in the development of fair and just regulations that are consistent with the law. We received over 1,900 written comments and verbal testimony from 5 public workshops. We are still reviewing and analyzing these comments, and it would be premature for us to address them at this point because our analysis is incomplete.

Please find enclosed a copy of the testimony that the MMS Director presented before the House Committee on Merchant Marine and Fisheries on this ANPR. I hope that it will be helpful to you. Please let me know if there is any way that I may be of further assistance.

Sincerely,

Cynthia Quarterman
Acting Director

Enclosure

cc: Chairman, Subcommittee on Coast Guard and Navigation
Merchant Marine and Fisheries Committee

Captain T. E. Omri, U.S. Coast Guard

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